SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1934

No. 17

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

vs.

LELAND POWERS, EXECUTOR, ET AL.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIRST CIRCUIT

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1 [Caption omitted.]

Before United States Board of Tax Appeals

DOCKET No. 47836

LELAND POWERS, EXECUTOR OF THE ESTATE OF SAMUEL L. POWERS, petitioner

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Appearances:

For taxpayer: Robert H. Montgomery, Esq., Melville F. Weston, Esq., Stanley R. Miller, Esq.

For Commissioner: Harold Allen, Esq.

Docket entries

1930

Mar. 13—Petition received and filed. Taxpayer notified (fee paid).
" 14—Copy of petition served on general counsel.
Apr. 24—Answer filed by general counsel.
May 1—Copy of answer served on taxpayer. General calendar.

2 1931

Feb. 11—Motion to consolidate with dockets 48007 and 51029 filed by taxpayer. 2/14/31 granted.

1932

Feb. 11—Hearing set April 27, 1932.
Mar. 31—Motion to consolidate with dockets 51029, 48007, and 50575 filed by taxpayer. 4/5/32 granted.
Apr. 27—Hearing had before Mr. Smith on merits. Submitted to Mr. Smith. Stipulation on facts filed. Briefs due in 30 days.
May 21—Brief filed by taxpayer.
" 27—Brief filed by general counsel.
Jun. 1—Transcript of hearing of April 27, 1932, filed.
Aug. 12—Order setting proceeding for hearing Sept. 14, 1932, for correction of the pleadings unless a stipulation is filed by the parties to the effect that the pleadings shall conform to the proof, entered.
Oct. 27—Findings of fact and opinion rendered, Charles P. Smith, div. 5. Judgment will be entered for the respondent.
" 27—Decision entered, Charles P. Smith, div. 5.
Dec. 22—Petition for review by U.S. Circuit Court of Appeals (1) with assignments of error filed by taxpayer.
" 22—Agreed statement of evidence lodged.

1933
Jan. 19—Praecipe filed—proof of service thereon.
" 20—Affidavit of service of petition for review filed.
" 20—Agreed statement of evidence approved and ordered filed.
Feb. 19—Order enlarging time to March 31, 1933, for transmission of record entered.

3 Before United States Board of Tax Appeals

Docket No. 51029

WINTHROP COFFIN, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Appearances:
For taxpayer: Robert H. Montgomery, Esq., M. F. Weston, Esq., S. R. Miller, Esq.
For Commissioner: Harold Allen, Esq.

Docket entries

1930
Nov. 28—Petition received and filed. Taxpayer notified. (Fee paid.)
" 28—Copy of petition served on general counsel.
1931
Jan. 6—Answer filed by general counsel.
" 17—Copy of answer served on taxpayer. General Calendar.
Feb. 11—Motion to consolidate with dockets 48007, 47836, and 50575 filed by taxpayer. 2/14/31 granted.
1932
Feb. 11—Hearing set April 27, 1932.
Mar. 31—Motion to consolidate with 61846, 47836, 51029, 48007, and 50575 filed by taxpayer.
Apr. 5—Motion granted.
(Memorandum. The remaining docket entries April 27, 1932, to February 19, 1933, being the same as docket entries in no. 47836 printed at page 1, are here omitted. A. I. Charron, clerk.)

4 Before United States Board of Tax Appeals

Docket No. 61846

HENRY I. HARRIMAN, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Appearances:
For taxpayer: Robert H. Montgomery, Esq., Melville F. Weston, Esq., Stanley R. Miller, Esq.
For Commissioner: Harold Allen, Esq.

Docket entries

1932

Feb. 11—Petition received and filed. Taxpayer notified. (Fee paid.)
" 12—Copy of petition served on general counsel.
Mar. 16—Answer filed by general counsel.
" 22—Copy of answer served on taxpayer. General Calendar.
" 31—Motion to consolidate with dockets 47836, 51029, 48007, and 50575 filed by taxpayer.
Apr. 4—Motion to file an amended answer filed by general counsel. Amended answer lodged.
" 5—Motion to consolidate granted.
" 7—Hearing set April 27, 1932.

(Memorandum. The remaining docket entries April 27, 1932 to February 19, 1933, being the same as docket entries in no. 47836 printed at page 1, are here omitted. A. I. Charron, clerk.)

5 Before U.S. Board of Tax Appeals

Docket No. 47836

[Title omitted.]

Petition

Filed March 13, 1930

The above-named petitioner hereby petitions for redetermination of the deficiency set forth by the Commissioner of Internal Revenue in the notice of deficiency (IT:AR:B–6 JMF–60D) dated February 21, 1930, addressed to Samuel L. Powers, 96 Arlington Street, Newton, Massachusetts, and as the basis of his proceeding alleges as follows:

1. The petitioner is the duly appointed and qualified executor of the Estate of Samuel L. Powers, late of Newton, Middlesex County, Massachusetts, and is a resident of said Newton (124 Chestnut Hill Road), a certificate of his appointment duly certified by the register of probate for said county is attached to the original of this petition, marked "Exhibit A" and a copy of said certificate is attached to each of the other copies hereof. Said Samuel L. Powers died November 30, 1929, and your petitioner was appointed executor as aforesaid on January 3, 1930. On or about March 10, 1930, your petitioner duly notified the Commissioner of Internal Revenue of his appointment as such. A copy of said notice is hereto attached marked "Exhibit B."

2. The notice of deficiency (copy of which is attached marked "Exhibit C") was mailed addressed to said Samuel L. Powers on February 21, 1930.

3. The taxes in controversy are income taxes for the calendar year 1927, and the amount in controversy is $553.44.

4. The determination of tax contained in said deficiency letter is based upon the following error:

The Commissioner has held that the taxpayer's salary as one of the trustees of the Boston Elevated Railway Company for the year 1927 is taxable.

5. The facts upon which the taxpayer relies as a basis of his appeal are as follows:

(a) On or about October 25, 1918, said Samuel L. Powers was appointed by the Governor of the Commonwealth of Massa-
6 chusetts, with the advice and consent of the Governor's council, a member of the board of trustees of the Boston Elevated Railway Company under the provisions of chapter 159 of the special acts of the General Court of said Commonwealth for 1928; on or about October 28, 1918, he took and subscribed to the oaths prescribed by the constitution and laws of said Commonwealth to qualify him to execute the trust imposed in him; said appointment was for a period of ten years from July 1, 1918; during the year 1927 he by virtue of said appointment acted as such trustee and received as compensation therefor the sum of $5,000, all pursuant to the terms of said special act.

(b) Pursuant to said special act the trustees took and had possession of the property of the Boston Elevated Railway Company in behalf of the Commonwealth, appointed and removed officers of the corporation, regulated and fixed fares, including the issuing, granting and withdrawal of transfers, determined the character and the extent of the services and facilities to be furnished, issued stock, bonds and other evidences of indebtedness, determined the amount of any deficiency resulting from the operation of the railway and notified the treasurer and receiver general of the Commonwealth thereof, whereupon it became the duty of the Commonwealth to pay over to the company the amount so ascertained, and apportioned among the cities and towns in which the railway was operated the taxes to be assessed upon them as an addition to the State tax wherewith to pay such deficiency, all as more fully appears in said special act to which reference is hereby made and a copy of which will be adduced in evidence. The jurisdiction of the Public Service Commission of the Commonwealth with respect to the fares, stock and bond issues, and facilities and services of the Boston Elevated Railway was terminated and transferred to said board of trustees.

6. Wherefore the petitioner prays for relief from the entire deficiency asserted by the respondent and that the Board may hear and redetermine said deficiency.

ROBERT H. MONTGOMERY,
Counsel for Petitioner,
30 Federal Street, Boston, Massachusetts.

7 [*Duly sworn to by Leland Powers, jurat omitted in printing.*]

COMMONWEALTH OF MASSACHUSETTS

Exhibit A to petition

Middlesex, ss:

Probate Court.

I, Loring P. Jordan, Register of the Probate Court for said County of Middlesex, hereby certify, that at a Probate Court holden in and for the said county, on the third day of January in the year of our Lord one thousand nine hundred and thirty the last will and testament of Samuel L. Powers, late of Newton in said county, deceased, testate, was duly proved and allowed in accordance with the laws of said Commonwealth, and letters testamentary thereon issued to Leland Powers of Newton in the county of Middlesex, the executor therein named who gave bond to the acceptance of the judge of said court for the due performance of said trust according to law.

I also certify, that it appears by the records and files of said court, that said letters are now in full force.

In witness whereof, I have hereunto set my hand and the seal of said court, this thirtieth day of January in the year of our Lord one thousand nine hundred and thirty.

[SEAL] LORING P. JORDAN, *Register.*

8 *Exhibit B to petition*

BOSTON, *March 10, 1930.*

COMMISSIONER INTERNAL REVENUE,
Washington, D.C.

DEAR SIR: Notice is hereby given that Mr. Samuel L. Powers, 96 Arlington Street, Newton, Massachusetts, died on November 30, 1929, and that the undersigned was duly appointed executor of his last will and testament on January 3, 1930. A certificate of his appointment is enclosed.

This notice is given pursuant to section 312 of the Revenue Act of 1928.

Very truly yours,

LELAND POWERS.

Address: 30 Federal Street, Boston, Mass.

Exhibit C to petition

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington, February 21, 1930.

Address reply to Commissioner of Internal Revenue and refer to IT:AR:B-6 JMF-60D.

Mr. SAMUEL L. POWERS,
96 Arlington Street, Newton, Massachusetts.

SIR: In accordance with section 274 of the Revenue Act of 1926, you are advised that the determination of your tax liability for the

year 1927 discloses a deficiency of $553.44, as shown in the statement attached.

The section of the law above mentioned allows you to petition the United States Board of Tax Appeals within sixty days (not counting Sunday as the sixtieth day) from the date of the mailing of this letter for a redetermination of your tax liability.

However(if you do not desire to petition, you are requested to execute the inclosed form 866 and forward both original and duplicate to the Commissioner of Internal Revenue, Washington, D.C., for the attention of IT:C:P–7. The signing of this agreement form will expedite the closing of your return by permitting an early assessment of any deficiencies and preventing the accumulation of interest charges, since the interest period terminates thirty days after filing the agreement form, or on the date assesssment is made, whichever is earlier; whereas if no agreement is filed, interest will accumulate to the date of assessment of the deficiencies.

Respectfully,

ROBT. H. LUCAS, *Commissioner.*
By *Deputy Commissioner.*

Inclosures: Statement. Form 866. Form 882.

STATEMENT

IT:AR:B–6. JMF–60D. FEB. 21, 1930.

In re: Mr. Samuel L. Powers, 96 Arlington Street, Newton, Massachusetts

Tax liability

Year	Corrected tax liability	Tax previously assessed	Deficiency
1927	$1,228.37	$674.93	$553.44

Information on file in this office discloses that you received a salary of $5,000.00 as one of five trustees for the State of Massachusetts of the Boston Elevated Railway Company, which amount was not reported in your return. Your protest executed October 25, 1929 against the deficiency proposed in office letter dated October 5, 1929 has been given consideration in the review of your return.

Net income reported	$20,671.82
Add: Salary from Boston Elevated Railway Company	5,000.00
Net income adjusted	25,671.82

The amount of $5,000.00 has been added to income reported for the reason it is held that the salary was not derived from the exercise of any essential governmental function as provided by section 213 (b) (7) of the Revenue Act of 1926, and article 88, Regulations

69. You are informed that to be entitled to the exemption provided by the Revenue Act of 1926 the services must have been rendered in connection with the exercise of an essential governmental function of the State or political subdivision. In this connection your attention is called to General Counsel Memorandum No. 3142, published in Cumulative Bulletin VII–1 at page 78.

Reference is made to the statement in issue 1 in the protest with respect to the years 1920 to 1923, inclusive, to the effect that in the Decision 12, United States Board of Tax Appeals 702, it was held that the trustees of the Boston Elevated Railway Company were officers of the Commonwealth of Massachusetts. It appears this decision was based upon the fact that the tax for the years mentioned was assessed under the provisions of section 1211 of the Revenue Act of 1926, which section required only that the services be rendered by an officer or employee of a State or political subdivision thereof. The question as to whether the services were rendered in the exercise of an essential governmental function, was not considered in arriving at the decision referred to.

With respect to issue 2 wherein it is contended that the trustees performed an essential governmental function, you are informed that the question has been given careful consideration, but in view of the circumstances surrounding the operation of the railway company, it is held by this office that services performed do not fall within the classification "Essential Governmental Function" as specified in article 88, Regulations 69. Your attention is called to Solicitor's Opinion 152, published in Cumulative Bulletin 2–2, page 93. The protest has, therefore, been denied.

Computation of tax

Net income adjusted		$25,671.82
Less: Dividends	$220.00	
Personal exemption	3,500.00	3,720.00
Balance subject to normal tax		21,951.82
Normal tax at 1½% on $4,000.00		60.00
Normal tax at 3% on $4,000.00		120.00
Normal tax on 5% on $13,951.82		697.59
11 Surtax on $25,671.82		557.06
Total		1,434.62
Less: Earned income credit		206.25
Tax liability		1,228.37
Tax previously assessed		674.93
Deficiency		553.44

Payment should not be made until a bill is received from the collector of internal revenue for your district and remittance should then be made to him.

You are advised that a copy of this communication has been transmitted to your representative Mr. Robert H. Montgomery, 30 Federal Street, Boston, Massachusetts, who has on file in this office a duly recorded power of attorney.

Before United States Board of Tax Appeals

Docket No. 47836

[Title omitted.]

Answer

Filed April 24, 1930

The Commissioner of Internal Revenue, by his attorney, C. M. Charest, general counsel, Bureau of Internal Revenue, for answer to the petition filed by above-named taxpayer, admits and denies as follows:

1. Admits the averments contained in paragraph 1.
2. Admits the averments contained in paragraph 2.
3. Admits the averments contained in paragraph 3.
4. Denies the error alleged in paragraph 4.
5. Admits the averments contained in paragraph 5 (a) and (b).

Wherefore, it is prayed that the taxpayer's petition be denied.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

Of counsel:

HAROLD ALLEN,
Special Attorney, Bureau of Internal Revenue.

12 Before United States Board of Tax Appeals

Docket No. 51029

[Title omitted.]

Petition

Filed November 28, 1930

The above-named petitioner hereby petitions for redetermination of the deficiency set forth by the Commissioner of Internal Revenue in the notice of deficiency IT: AR B–1 MCB–60D) dated November 17, 1930, and as the basis of his proceeding alleges as follows:

1. The petitioner is a resident of Brookline, 45 Warren Street, Norfolk County, Massachusetts.

2. The notice of deficiency, copy of which is attached marked "Exhibit A", was mailed on November 17, 1930.

3. The taxes in controversy are income taxes for the calendar year 1927 and the amount in controversy is $934.29.

4. The determination of tax assessed in said deficiency letter is based upon the following error: "The Commissioner has held that the taxpayer's salary as one of the trustees of the Boston Elevated Railway Company for the year 1927 is taxable."

5. The facts upon which the taxpayer relies as the basis of his appeal are as follows:

(a) Prior to the year 1927 the taxpayer was appointed by the Governor of the Commonwealth of Massachusetts, with the advice and consent of the Governor's council, a member of the board of trustees of the Boston Elevated Railway Company under the provisions of chapter 159 of the Special Acts of the General Court of said Commonwealth for 1918; prior to said year 1927 he took and subscribed to the oath prescribed by the Constitution and laws of said Commonwealth qualifying him to execute the trust imposed in him; said appointment was for a period expiring ten years from
13 July 1, 1918; during the year 1927 he by virtue of said appointment acted as such trustee and received as compensation therefor the sum of $5,000, all pursuant to the terms of said special act.

(Memorandum. The remaining paragraphs 5 (b) and 6, being the same as those of the petition in no. 47836, already printed at pages 5 and 6, are here omitted. A. I. Charron, clerk.)

ROBERT H. MONTGOMERY,
Counsel for Taxpayer,
30 Federal Street, Boston, Mass.

[*Duly sworn to by Winthrop Coffin, jurat omitted in printing.*]

Exhibit A to petition

Mailed Nov. 17, 1930.

IT:AR:B–1 MCB–60D

Mr. WINTHROP COFFIN,
(c/o Coffin and Burr, Incorporated),
60 State Street, Boston, Massachusetts.

SIR: You are advised that the determination of your tax liability for the year(s) 1927 discloses a deficiency of $934.29, as shown in the statement attached.

In accordance with section 274 of the Revenue Act of 1926, notice is hereby given of the deficiency mentioned. Within sixty days (not counting Sunday as the sixtieth day) from the date of the mailing of this letter, you may petition the United States Board of Tax Appeals for a redetermination of your tax liability.

However, if you do not desire to petition, you are requested
14 to execute the enclosed agreement form and forward it to the Commissioner of Internal Revenue, Washington, D.C., for the attention of IT:C:P–7. The signing of this agreement will expedite the closing of your return(s) by permitting an early assessment of any deficiency and preventing the accumulation of interest charges, since the interest period terminates thirty days after filing

the enclosed agreement, or on the date assessment is made, whichever is earlier; whereas if no agreement is filed, interest will accumulate to the date of assessment of the deficiency.

Respectfully,

DAVID BURNET,
Commissioner.
By W. T. SHERWOOD,
Acting Deputy Commissioner.

Enclosures: Statement. Form 882. Form 870.

STATEMENT

IT:AR:B–1 MCB–60D

In re: Mr. Winthrop Coffin, c/o Coffin and Burr, Incorporated, 60 State Street, Moston, Massachusetts

Tax liability

Year	Corrected tax liability	Tax previously assessed	Deficiency
1927	$10,148.17	$9,213.88	$934.29

Further reference is made to the review of your 1927 income tax return in connection with the report of the internal revenue agent in charge, Boston, Massachusetts, covering an examination of your income tax liability for the year in question.

The issue involved is the taxability of money received for services rendered as trustee of the Boston Elevated Railway Company.

You are advised that this office holds that the salary received by you as trustee of the Boston Elevated Railway Company was not for services rendered in the exercise of an essential governmental function and is subject to Federal income tax.

The report of the internal revenue agent in charge, Boston, Massachusetts, covering an examination of your 1927 income
15 tax liability, a copy of which was furnished you, has been reviewed and approved by this office, with the following exception:

The amount previously assessed is $9,213.88 instead of $9,212.17, as shown by the revenue agent's report.

A synopsis of your return as corrected, follows:

Net income reported on the return	$86,105.90
Plus: 1. Salary	5,009.00
Adjusted net income	91,105.94

Less:		
Dividends	$88,837.00	
Personal exemption	4,700.00	
		$91,537.00
Balance subject to normal tax		None
Surtax on $91,105.94		9,970.13
Tax at 12½% on capital net gain of $2,014.78		251.84
Total tax		10,221.97
Less:		
Credit of 25% for earned net income	14.00	
Tax paid at source	59.80	
		73.80
Total tax assessable		10,148.17
Tax previously assessed		9,213.88
Deficiency		934.29

EXPLANATION OF CHANGES

Salary of $5,000.00 received as trustee of the Boston Elevated Railway Company has been added to your taxable income for reasons as explained above.

A copy of this communication has been furnished your attorney, Mr. Robert H. Montgomery, who has on file in this office, a duly recorded power of attorney.

Payment should not be made until a bill is received from the collector of internal revenue for your district and remittance should then be made to him.

16 Before United States Board of Tax Appeals

Docket No. 51029

[Title omitted.]

Answer

Filed January 6, 1931

The Commissioner of Internal Revenue, by his attorney C. M. Charest, general counsel, Bureau of Internal Revenue, for answer to the petition filed by above-named taxpayer, admits and denies as follows:

1, 2, 3. Admits the averments contained in paragraphs 1, 2, and 3.

4. Denies error in the action recited in paragraph 4.

5. Admits the averments contained in paragraph 5.

Wherefore, it is prayed that the taxpayer's petition be denied.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

Of counsel:

HAROLD ALLEN,
Special Attorney, Bureau of Internal Revenue.

Before United States Board of Tax Appeals

Docket No. 61846

[Title omitted.]

Petition

Filed February 11, 1932

The above-named petitioner hereby petitions for redetermination of the deficiency set forth by the Commissioner of Internal Revenue in the notice of deficiency (IT:AR:B–1:ARM–60D) dated January 14, 1932 and as the basis of his proceeding alleges as follows:

1. The petitioner is a resident of Newton, in the county of Middlesex, and Commonwealth of Massachusetts, residing at 825 Centre Street in said Newton.

2. The notice of deficiency, copy of which it attached marked "Exhibit A" was mailed on January 14, 1932.

17 3. The taxes in controversy are income taxes for the calendar year 1929 and the amount in controversy is $955.66.

4. The determination of tax proposed to be assessed in said deficiency letter is based upon the following error: The sustaining by the Commissioner of the action of the examining officer in including the salary of $5,000 received by the taxpayer in the year 1929 as one of the trustees of the Boston Elevated Railway Company as part of the taxpayer's taxable income for the year 1929.

5. The facts upon which the taxpayer relies as the basis of his appeal are as follows:

(a) Prior to the year 1929 the taxpayer was appointed by the Governor of the Commonwealth of Massachusetts, with the advice and consent of the Governor's counsel, a member of the Board of Trustees of the Boston Elevated Railway Company under the provisions of chapter 159 of the Special Acts of the General Court of said Commonwealth of the year 1918; prior to said year 1929 he took and subscribed to the oath prescribed by the constitution and laws of said Commonwealth qualifying him to execute the trust so imposed in him; said appointment was for a term which included in its entirety the said year 1929, and during the said year 1929 he by virtue of said appointment acted as such trustee and received as compensation therefor the sum of $5,000, all pursuant to the terms of said special act.

[MEMORANDUM. The remaining paragraphs 5 (b) and 6, being the same as those of the petition in no. 47836, already printed at pages 5 and 6, are here omitted. A. I. Charron, clerk.]

ROBERT H. MONTGOMERY,
MELVILLE F. WESTON,
Counsel for Taxpayer,
30 Federal Street, Boston, Mass.

[*Duly sworn to by Henry I. Harriman, jurat omitted in printing.*]

18 Amendment to Petition. Filed August 20, 1932

Exhibit "A" to petition

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington, Jan. 14, 1932.

Address reply to Commissioner of Internal Revenue and refer to Mr. HENRY I. HARRIMAN,
825 Centre Street, Newton, Massachusetts.

SIR: You are advised that the determination of your tax liability for the year(s) 1929 discloses a deficiency of $955.66, as shown in the statement attached.

In accordance with section 272 of the Revenue Act of 1928, notice is hereby given of the deficiency mentioned. Within sixty days (not counting Sunday as the sixtieth day) from the date of the mailing of this letter, you may petition the United States Board of Tax Appeals for a redetermination of your tax liability.

However, if you do not desire to petition, you are requested to execute the enclosed agreement form and forward it to the Commissioner of Internal Revenue, Washington, D.C., for the attention of IT:C:P-7. The signing of this agreement will expedite the closing of your return(s) by permitting an early assessment of any deficiency and preventing the accumulation of interest charges, since the interest period terminates thirty days after filing the enclosed agreement, or on the date assessment is made, whichever is earlier; whereas if no agreement is filed, interest wil accumulate to the date of assessment of the deficiency.

Respectfully,

DAVID BURNET,
Commissioner.
By J. C. WILMER,
Deputy Commissioner.

Enclosures: Statement. Form 882. Form 870.

IT:AR:B-1 ARM-60D

19 STATEMENT

In re: Mr. Henry I. Harriman, 825 Centre Street, Newton, Massachusetts

Tax liability

Years	Tax liability	Tax assessed	Deficiency
1929	$15,072.09	$14,116.43	$955.66

The adjustent recommended in the report of the internal revenue agent in charge at Boston, Massachusetts, a copy of which was furnished you, has been approved after considering your protest.

You contend that salary of $5,000.00 received for services rendered as trustee of the Boston Elevated Railway Company is exempt from tax and that your return should be adjusted in accordance with the decision rendered in the case of Winthrop Coffin et al., 12 United States Board of Tax Appeals, page 702.

You are advised that the decision rendered in the above case applied to the taxable years 1921 and 1923, inclusive, whereas, article 643 of Regulations 74 reads in part as follows:

"Compensation paid to its officers and employees by a State or political subdivision thereof for services rendered in connection with the exercise of an essential governmental function of the State or political subdivision, including fees received by notaries public commissioned by States, is not taxable. Compensation received for services rendered to a State or political subdivision thereof is included in gross income unless (a) the person receives such compensation as an officer or employee of a State or political subdivision, and (b) the services are rendered in connection with the exercise of an essential governmental function. . . .

"An officer is a person who occupies a position in the service of the State or political subdivision, the tenure of which is continuous and not temporary and the duties of which are established by law or regulations and not by agreement. An employee is one whose duties consist in the rendition of prescribed services and not the accomplishment of specific objects, and whose services are continuous, not occasional or temporary. . . ."

In Mimeograph 3838 published in Cumulative Bulletin IX–2, page 137, it is stated,

"Street railways.—While the operation of a street railway may be a public necessity, it is not an instrumentality of the city in the discharge of its ordinary functions as a government. If it is not an instrumentality of government, it is not, in accordance with the decisions quoted above, removed from the sphere of Federal taxation, and the compensation of the officers and employees thereof must be included in gross income. (See Sol. Op. 152, C.B. Dec. 1923, p. 93; S.M. 2232 C.B. Dec. 1924, p. 83; I.T. 2405, C.B. June 1928, p. 72; City of Seattle et al. *v.* Poe, Collector, et al., 4 Fed. (2d) 276 (5 Am. Fed. Tax. Rep. 5329), T.D. 3701, C.B. June 1925, p. 290.)"

In view of the above, the action of the examining officer in including the salary of $5,000.00 received as trustee of the Boston Elevated Railway Company as income taxable under the Revenue Act of 1928 is sustained.

Net income reported on return	$112,352.16
Add: Salary	5,000.00
Net income adjusted	117,352.16

COMPUTATION OF TAX

Net income adjusted		$117,352.16
Less:		
Dividends	$111,676.75	
Personal exemption and credit for dependent	3,900.00	
		115,576.75
Income subject to normal tax		1,775.41
Normal tax at ½% on $1,775.41		8.88
21 Surtax on $117,352.16		$15,130.43
Total tax		15,139.31
Les: Earned income credit		67.22
Tax assessable		15,072.09
Tax previously assessed		14,116.43
Deficiency in tax		955.66

Since no reply has been received to office letter dated December 17, 1931, this letter of final determination is being issued.

Before United States Board of Tax Appeals

Docket No. 61846

[Title omitted.]

Answer

Filed March 16, 1932

The Commissioner of Internal Revenue, by his attorney, C. M. Charest, general counsel, Bureau of Internal Revenue, for answer to the petition filed in the above-entitled appeal, admits and denies as follows:

1. Admits the allegations contained in paragraph 1 of the petition.

2. Admits that the notice of deficiency was mailed January 14, 1932.

3. Admits the taxes in controversy are income taxes for the calendar year 1929, but denies that the amount in controversy is $955.66.

4. Denies that the respondent erred in the manner alleged in paragraph 4 of the petition.

5. (a) and (b). Admits that the petitioner received in the year 1929 the sum of $5,000 for services rendered as trustee of the Boston Elevated Railway Company, and denies the remaining allegations contained in subparagraphs (a) and (b) of paragraph 5 of the petition.

22 Denies generally and specifically each and every allegation contained in the petition not hereinbefore admitted, qualified, or denied.

Wherefore, it is prayed that the Board redetermine the amount of the deficiency involved in this proceeding to be equal to the amount determined by the Commissioner, plus any additional amount

which may arise from the correction of any error or errors that may have been committed by the Commissioner. Claim is hereby asserted for the increased deficiency, if any, resulting from such redetermination.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

Of counsel:
C. A. RAY,
Special Attorney, Bureau of Internal Revenue.

Before United States Board of Tax Appeals

Docket No. 61846

[Title omitted.]

Amended answer

Filed April 11, 1932

The Commissioner of Internal Revenue, by his attorney, C. M. Charest, general counsel, Bureau of Internal Revenue, for amended answer to the petition filed by above-named taxpayer, admits and denies as follows:

1, 2, and 3. Admits the averments contained in paragraphs 1, 2, and 3.

4. Denies error in the action stated in paragraph 4.

5. Admits the averments contained in paragraph 5.

Wherefore, it is prayed that the Board redetermine the amount of the deficiency involved in this proceeding to be equal to the amount determined by the Commissioner, plus any additional amount which may arise from the correction of any error or errors that may have been committed by the Commissioner. Claim is hereby asserted for the increased deficiency, if any, resulting from such redetermination.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

23 Of counsel:
HAROLD ALLEN,
Special Attorney, Bureau of Internal Revenue.

Before United States Board of Tax Appeals

LELAND POWERS, EXECUTOR OF THE ESTATE OF SAMUEL L. POWERS, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

STANLEY R. MILLER, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

WINTHROP COFFIN, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

HENRY I. HARRIMAN, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Docket Nos. 47836, 48007, 50575, 51029, 61846

Compensation paid to the petitioners as trustees of the Boston Elevated Railway Company during the taxable years 1926 to 1929, inclusive, held, subject to Federal income tax.

Melville F. Weston, Esq., and Stanley R. Miller, Esq., for the petitioners.

Harold Allen, Esq., for the respondent.

Findings of fact and opinion

Promulgated October 27, 1932

These proceedings, duly consolidated for hearing, are for the redetermination of deficiencies in income tax for the years and in amounts as follows:

Docket No.	Petitioner	Year	Deficiency
47836	Leland Powers, executor of the estate of Samuel L. Powers	1927	$553.44
48007	Stanley R. Miller	1926	240.89
		1927	334.36
24 50575	Stanley R. Miller	1928	226.02
51029	Winthrop Coffin	1927	994.29
61846	Henry I. Harriman	1929	965.66

For convenience, Docket No. 47836 will be treated as though the decedent, whose income is in issue, were the petitioner. The petitioners allege that the respondent erred in including in their taxable

incomes the compensation each received as a trustee of the Boston Elevated Railway Company for the respective years. The proceedings were submitted upon the pleadings and stipulations.

Findings of fact

The petitioners are residents of the Commonwealth of Massachusetts.

Prior to the taxable years under consideration, the petitioners were appointed members of the board of trustees of the Boston Elevated Railway Company under the provisions of Chapter 159 of the Special Acts of 1918 of the Commonwealth of Massachusetts, "An act to provide for the public operation of the Boston Elevated Railway Company," which reads in part as follows:

"SECTION 1. The board of trustees of the Boston Elevated Railway Company is hereby created, to consist of five persons to be appointed by the governor, with the advice and consent of the council. The persons so appointed shall be sworn before entering upon the performance of their duties; shall own no stock or other securities of the Boston Elevated Railway Company or of any company owned, leased, or operated by it; shall serve for the term of ten years from the date when they assume the management of the company as hereinafter provided and until their successors are duly appointed and qualified; and *each shall receive from the company as compensation for his services five thousand dollars annually.* . . .

"*Said trustees shall not be considered public officers within the meaning of section twenty-five of chapter five hundred and fourteen of the acts of nineteen hundred and nine*, but shall be subject in all other respects to the provisions of said section to the same extent as are the directors of the Boston Elevated Railway Company, but said section shall not apply to recommendations by the governor to said trustees. . . .

"If the public management and operation of the railway system of the Boston Elevated Railway Company shall continue beyond the original period of ten years the governor shall, with the advice and consent of the council, at the expiration of each ten-year period during the continuance of public management and operation, appoint five successor trustees to serve for a period of ten years, and until their successors are appointed and qualified, but not exceeding the period of public management and operation. . . .

"SECTION 2. *Said board of trustees*, hereinafter called the trustees, *shall manage and operate the Boston Elevated Railway Company*, hereinafter called the company, and the properties owned, leased, or operated by it, for a period of ten years, commencing on the first day of the month next after their appointment and qualification, and subject to the provisions of this act, shall take and have possession of said properties in behalf of the Commonwealth during the period

of public operation, and, for the purposes of this act, shall, except as is otherwise provided in this act, have and may exercise all the rights and powers of said company and its directors, and, upon behalf of said company, shall receive and disburse its income and funds. . . . They shall have the right to regulate and fix fares, including the issue, granting, and withdrawal of transfers, and the imposition of charges therefor, and shall determine the character and extent of the service and facilities to be furnished, *and in these respects their authority shall be exclusive and shall not be subject to the approval, control, or direction of any other State board or commission.*

In the management and operation of the said company and of the properties owned, leased, or operated by it, as authorized by this act, the *trustees* and their agents, servants, and employees *shall be deemed to be acting as agents of the company and not of the Commonwealth*, and the company shall be liable for their acts and negligence in such management and operation to the same extent as if they were in the immediate employ of the company, but said trustees shall not be personally liable. . . . Nothing herein contained shall be held to affect the right of the Commonwealth or any subdivision thereof to tax the company or its stockholders in the same manner and to the same extent as if the company had continued to manage and operate its own property.

"SECTION 3. The trustees shall have authority to make contracts in the name and on behalf of, and to issue stocks, bonds, and other evidences of indebtedness of, the company. . . .

". . . The trustees shall cause to be paid all amounts which may from time to time become due from the company, and shall declare dividends at the appointed times upon the preferred and common stock of the company, and provide for the payment of the same. . . .

"SECTION 6. The trustees shall from time to time, in the manner hereinafter provided, fix such rates of fare as will reasonably insure sufficient income to meet the cost of the service, which shall include operating expenses, taxes, rentals, interest on all indebtedness, such allowance as they may deem necessary or advisable for depreciation of property and for obsolescence and losses in respect to property sold, destroyed, or abandoned, all other expenditures and charges which under the laws of the Commonwealth now or hereafter in effect may be properly chargeable against income or surplus, fixed dividends on all preferred stock of the company from time to time outstanding, and dividends on the common stock of the company from time to time outstanding at the rate of five per cent per annum on the par value thereof during the first two years, five and one-half per cent per annum on the par value thereof during
27 the next two years and six per cent per annum on the par value thereof during the balance of the period of public operation. . . .

"SECTION 11. If, as of the last day of June in the year nineteen hundred and nineteen, or the last day of any December or June thereafter, the amount remaining in the reserve fund shall be insufficient to meet the deficiency mentioned in section nine, it shall be the duty of the trustees to notify the treasurer and receiver general of the Commonwealth of the amount of such deficiency, less the amount, if any, in the reserve fund applicable thereto, and the Commonwealth shall thereupon pay over to the company the amount so ascertained. . . . If, as of the last day of any June or December thereafter during the period of public operation, the reserve fund shall exceed the amount originally established, the trustees shall apply the excess, so far as necessary, to reimbursing the Commonwealth for any amounts which it may have paid to the company under the provisions hereof, and the Commonwealth shall thereupon distribute the amount so received among the cities and towns in which the company operates, in proportion to the amounts which they have respectively been assessed as provided in section fourteen. . . .

"SECTION 12. Notwithstanding anything contained in this act, *the public management and operation of the railway system of the company* shall continue after the expiration of said ten-year period upon the terms and conditions herein specified until such time as the Commonwealth shall elect to discontinue such public management and operation. The Commonwealth shall have the right to terminate such public management and operation, either at the expiration of the said ten-year period or at any time thereafter, by appropriate legislation passed not less than two years before the date fixed for such termination.

"SECTION 13. It shall be the duty of the trustees to maintain the property of the company in good operating condition and to make such provision for depreciation, obsolescence, and rehabilita-
28 tion, that, upon the expiration of the period of public management and operation, the property shall be in good operating condition. If the period of public management and operation expires, control of the property shall then revert to the company, and if at that time the reserve fund shall be less than the amount originally established because the income during the period of public management and operation has been insufficient to pay the cost of the service, the Commonwealth shall forthwith pay over to the company an amount sufficient to restore it to its original amount, and if the amount in said reserve fund is then in excess of the amount originally established and any amount required to meet the cost of the service to the expiration of such period, such excess shall be paid into the treasury of the Commonwealth and distributed among the cities and towns in which the company operates in the same proportions as the assessments provided for by section fourteen.

"SECTION 14. In case the Commonwealth shall be called upon to pay to the trustees or the company any amount under the provisions

of sections eleven and thirteen, such amount with interest or other charges incurred in borrowing money for the purpose shall be assessed upon the cities and towns in which the company operates by an addition to the State tax next thereafter assessed in proportion to the number of persons in said cities and towns using the service of the company at the time of said payment, said proportion to be determined and reported to the treasurer and receiver general by the trustees from computations made in their discretion for the purpose.

"SECTION 15. Upon the termination of the period of public management and operation, the company shall manage and operate the property and may fix and collect such just and reasonable fares as will produce an income sufficient to pay the reasonable cost of the service as defined in section six, including dividends upon the common stock from time to time outstanding of six per cent per annum on the par value thereof but no more, and may establish
29 schedules of fares which shall automatically increase or decrease in the same manner as is authorized in the case of the trustees: provided, that the Commonwealth shall be under no liability to make any payments to the company by reason of any deficiencies in income accruing after the discontinuance of public operation. The company shall thereafter be subject to public regulation and supervision in such manner as may be determined by the general court, but such regulation and supervision shall not be exercised so as to reduce the income below the reasonable cost of the service as defined in this act." [Italics supplied.]

In 1919, the Commonwealth, pursuant to the terms of section 11 of chapter 159, paid over to the company $3,980,151.67, the amount of the deficiency resulting from the public operation of the railway; this sum was apportioned among the cities and towns served by the railway as an addition to the State tax. Subsequent operations of the railway up to and including 1929 did not result in an excess of income sufficient to fully reimburse the Commonwealth and/or the cities and towns for the amount paid to the company in 1919.

During the respective taxable years each petitioner was a member of the board of trustees of the Boston Elevated Railway Company and as such trustee received compensation from the Railway Company in the amount of $5,000 per year as provided in chapter 159 of the Special Acts of 1918.

The Commissioner has determined that the compensation thus received by each petitioner is subject to income tax in the respective taxable years.

Opinion

SMITH: In Winthrop Coffin, 12 B.T.A. 702, this Board held that compensation paid to trustees of the Boston Elevated Railway Company in the years 1920 to 1923, inclusive, was exempt from the Federal income tax. We there considered this issue solely from the standpoint of whether the taxpayers were officers of the Com-

30 monwealth of Massachusetts. After a full consideration of the legislation creating the board of trustees for the operation of the Boston Elevated Railway Company and pertinent court decisions relating thereto, we said:

"We are led to the inescapable conclusion that the petitioners are officers of the Commonwealth of Massachusetts. In view of section 1211 of the Revenue Act of 1926 which makes that the test of exemption, we do not deem it necessary to discuss the question as to whether the services performed by the trustees are essentially governmental or not. As we construe section 1211, that question need not be answered if the petitioners are receiving amounts 'as compensation for personal services as an officer or employee of any State.' We see no escape from holding that the salaries of the petitioners were so received and we, therefore, hold that such salaries are exempt from tax."

The respondent now contends that although the petitioners were officers of the Commonwealth of Massachusetts, the compensation they received as members of the board of trustees of the Boston Elevated Railway Company is, nevertheless, subject to the Federal income tax, since their duties did "not involve the exercise of an essentially governmental function", citing Flint v. Stone Tracy Co., 220 U.S. 107. See also article 88 of Regulations 69, and article 643 of Regulations 74.

On brief, the petitioners call attention to the fact that neither the Revenue Act of 1926 nor the Revenue Act of 1928 contains an express provision with respect to this type of exemption, which the Commissioner's Regulations purport to limit to the compensation for services rendered "in connection with the exercise of an essential governmental function."

The petitioners contend that the public operation of the Boston Elevated Railway Company was not the exercise of a proprietary right but of an essential governmental function; that in any event the board of trustees was a special public service commission for that railway, and as such engaged in an essential governmental function; and further, that the taxation of the compensation
31 here involved "constitutes an undue interference with the workings of the State Government."

The Supreme Court has recently considered the question of tax exemption of instrumentalities of the Federal Government and in Fox Film Corporation v. Doyal et al., — U.S. — (decided May 16, 1932), said:

"The principal of the immunity from State taxation of instrumentalities of the Federal Government, and of the corresponding immunity of State instrumentalities from Federal taxation—essential to the maintenance of our dual system—has its inherent limitations. It is aimed at the protection of the operations of government (McCullough v. Maryland, 4 Wheat. 316, 436), and the immunity does not extend 'to anything lying outside or beyond governmental

functions and their exertions.' Indian Motorcycle Co. v. United States, 283 U.S. 570, 576, 579. Where the immunity exists, it is absolute, resting upon 'an entire absence of power' (Johnson v. Maryland, 254 U.S. 51, 55, 56), but it does not exist 'where no direct burden is laid upon the governmental instrumentality and there is only a remote, if any, influence upon the exercise of the functions of government.' Willcuts v. Bunn, 282 U.S. 216, 225."

In Group No. 1 Oil Corporation v. Bass, 283 U.S. 279, 51 Sup.Ct. 432, 433, the Supreme Court pointed out that the immunity there contended for and applicable here, did not extend to a "nondiscriminatory tax" imposed by one government that remotely and indirectly affects another government.

The principal of immunity referred to in Fox Film Corporation v. Doyal et al., supra, had its genesis in McCullough v. State of Maryland, 4 Wheat. 316, wherein the Supreme Court held unconstitutional a discriminatory tax laid by the State of Maryland "on all banks or branches thereof in the State of Maryland, not chartered by the legislature." The facts of that case are too familiar to require further recital here. The principle there established has received elucidation by the Supreme Court in recent tax
32 cases in which it has reconsidered the principle of immunity and the nature of its "inherent limitations." See Fox Film Corporation v. Doyal et al., supra; Group No. 1 Oil Corporation v. Bass, supra; Indian Motorcycle Co. v. United States, 283 U.S. 570, 51 S.Ct. 601; Burnet v. Coronado Oil & Gas Co. — U.S. —, 52 S.Ct. 443.

There is no discrimination in the imposition of the tax in controversy, which is laid upon the net income of individuals, determined after certain credits and deductions from gross income, which includes "gains, profits, and income derived from salaries, wages, or compensation for personal service . . . of whatever kind, and in whatever form paid." Sections 210 to 213 of the Revenue Act of 1926, and sections 11, 12, 21 and 22 of the Revenue Act of 1928. And, as the Supreme Court said in Willcuts v. Dunn, 282 U.S. 216, 51 S.Ct. 125, 129:

". . . It must be remembered that we are dealing, not with any express constitutional restriction, but only with an asserted implication. The constitutional provisions authorizing the Congress to lay taxes (article 1, § 8, sixteenth amendment) are certainly broad enough to cover the tax in question. . . ."

Tax exemptions are never lightly to be inferred (Heiner v. Colonial Trust Co., 275 U.S. 232), must be given a practical construction such "as will not unduly impair the taxing power" of the Federal Government "or the appropriate exercise of its functions" by the State government (Susquehanna Co. v. Tax Commission, 283 U.S. 291, 294), and the constitutional exemption, if any, must be construed strictly against the taxpayer. (Pacific Company, Ltd., v. Johnson, — U.S. —, April 11, 1932.) The exemption claimed in

the instant proceedings, since there is no express statutory provision therefor, cannot be determined "apart from the purpose and character of the legislation" by which the Commonwealth of Massachusetts undertook the operation of the Boston Elevated Railway Company through a board of trustees, of which the petitioners were members. Cf. Shaw v. Oil Corporation, 276 U.S. 575, 578.

In Winthrop Coffin, supra, we found that the trustees of the
33 Boston Elevated Railway Company were officers of the Commonwealth of Massachusetts, despite the provisions of section 1 of chapter 159 of the Special Acts of 1918, which declared that the trustees "shall not be considered public officers." This conclusion was based upon other provisions of the act than section 1, and upon the interpretations placed thereon by the Supreme Court of Massachusetts. That determination is not dispositive of the issue now before us, since there the exemption claimed was found to be within section 1211 of the Revenue Act of 1926, which has no application to the years now in controversy. In section 2 of chapter 159 of the Special Acts of 1918, it is provided that the trustees "shall be deemed to be acting as agents of the company and not of the Commonwealth" and that the company remained liable for their acts just as if they were in the immediate employ of the company. In the opinion of the justices of the Supreme Judicial Court of Massachusetts, rendered April 2, 1919, and reported at 231 Mass. 603; 122 N.E. 763, 765, is the following:

". . . In essence Special Acts 1918, c. 159, was a legislative agreement for the lease to the commonwealth of a public utility to be operated for a limited time by public officers upon the payment of fair rental on an investment made under public supervision and under laws prohibiting stock watering or other means of inflation.

"We are led to the conclusion that said chapter 159 was within the constitutional power of the legislature."

In interpreting the provision of chapter 159 under which the trustees apportioned the amount to be assessed against certain cities and towns served by the railway and collected from such cities and towns as an addition to the State tax assessed, the Supreme Court of Massachusetts, in City of Boston *v.* Treasurer and Receiver General, 237 Mass. 403, 130 N.E. 390, affirmed its earlier opinion regarding chapter 159 of the Special Acts of 1918, and held constitutional section 14 of the act by which the deficiency in the earnings under sections 11 and 13 were assessed against the cities and towns served by the railway. In the course of that opinion the court said:

34 "Some analysis of the provisions of Sp. St. 1918, c. 159, is necessary in order to deal with the contentions that it is unconstitutional. Its general scope is indicated by its title, which is "An act to provide for the public operation of the Boston Elevated Railway Company." The accuracy of the title is confirmed by the substance of the act throughout. Its purpose is operation through public officers and not public ownership. . . ."

The court also stated that the Commonwealth had the constitutional power to assume the management and operation of the Boston Elevated Railway Company. But nowhere does the court undertake to say that the Commonwealth of Massachusetts was thereby engaged in an esential governmental function, although it upheld the tax levied under section 14 of the act on the grounds that the tax was levied for a public purpose. See also City of Chelsea *v.* Treasurer and Receiver General, 237 Mass. 422, 130 N.E. 397; Boston *v.* Jackson, 260 U.S. 309. In the opinion of the justices, rendered November 22, 1927, reported 159 N.E. 70, it appears that the corporate entity remained intact and that the property remained the property of the Boston Elevated Railway Company.

In January 1925 the Justices of the Supreme Judicial Court of Massachusetts rendered an opinion, reported 148 N.E. 889, 891, pointing out that the Commonwealth or local government had the power to acquire or construct instrumentalities for public travel and to charge toll, rental, or other recompense therefor (citing Commonwealth *v.* Wilkinson, 16 Pick. 175); such powers resting on the rights of the Commonwealth as proprietor of the instrumentalities used. Thus, it appears that in the opinion of the justices, rendered in connection with a question involving certain tunnels constructed by the city of Boston and leased to the Boston Elevated Railway Company, such instrumentalities are constructed and operated in the exercise of a proprietary right. Furthermore, regardless of the operation of the railway by the Commonwealth, the Supreme Court of Massachusetts has held the Boston Elevated Railway Company liable for damages during this period of operation. See Harter *v.* Boston Elevated Railway Co., 156 N.E. 543 (May 1927).

From a consideration of the above opinions pertaining to the legislation by which the Commonwealth of Massachusetts took over the operation of the Boston Elevated Railway, we conclude that chapter 159 of the Special Acts of 1918 was for a "public purpose" (which term is not synonymous with "governmental purpose", see T. P. Wittschen, 25 B.T.A. 46, 52), and for the time provided deprived the private corporation of the exercise of its proprietary rights and gave them to the board of trustees.

In Flint *v.* Stone Tracy Co., supra, the question of tax exemption was reviewed at length and governmental agencies and functions fully discussed. The Supreme Court, in considering the question of exemption as it related to public-service corporations, to wit, two rapid-transit corporations comparable to the Boston Elevated Railway Company, said:

". . . In the case of South Carolina *v.* United States, 199 U.S. 437, 50 L.ed. 261, 26 Sup. Ct. Rep. 110, 4 A. & E. Ann. Cas. 737, this court held that when a State, acting within its lawful authority, undertook to carry on the liquor business, it did not withdraw the agencies of the State, carrying on the traffic, from the operation of the internal revenue laws of the United States. If a State may

not thus withdraw from the operation of a Federal taxing law a subject-matter of such taxation, it is difficult to see how the incorporation of companies whose service, though of a public nature, is nevertheless, with a view to private profit, can have the effect of denying the Federal right to reach such properties and activities for the purposes of revenue.

"It is no part of the essential governmental functions of a State to provide *means of transportation*, supply artificial light, water, and the like. These objects are often accomplished through the medium of private corporations, and though the public may derive a benefit from such operations, the companies carrying on such enterprises are nevertheless private companies, whose business
36 is prosecuted for private emolument and advantage. For the purpose of taxation they stand upon the same footing as other corporations upon which special franchises have been conferred.

"The true distinction is between the attempted taxation of those operations of the States *essential* to the execution of its governmental functions, and which the State *can only do itself*, and those activities which are of a private character. The former, the United States may not interfere with by taxing the agencies of the State in carrying out its purposes; the latter, although regulated by the State, and exercising delegated authority, such as the right of eminent domain, are not removed from the field of legitimate Federal taxation." [Italics supplied.]

The petitioners rely upon the decision of the Circuit Court of Appeals for the First Circuit in Jamestown & Newport Ferry Co. *v.* Commissioner, 41 Fed. (2d) 920, wherein the Ferry Company was held to be an instrumentality of government and not subject to the Federal income tax. That case is distinguishable from the proceedings at bar in that there the income from a public utility (the ferry), accrued to a political subdivision of a State and was specifically exempted from Federal taxation by section 213 (b) (7) of the Revenue Acts of 1921 and 1924. There, the ferry corporation was owned and operated by a town located on an island. Likewise, the decision of the Circuit Court of Appeals for the Ninth Circuit in United States *v.* King County, Wash., et al., 281 Fed. 686, is cited and relied upon. There the county owned and operated a ferry which the court held exempt from the transportation tax imposed by section 500 of the Revenue Act of 1917. In both cases there was a direct burden upon or interference with a political subdivision of a State. Likewise, the decision of the District Court for the Eastern District of Michigan in Frey *v.* Woodworth, 2 Fed. (2d) 725, is distinguishable in that the exemption granted applied to the income of an employee of a municipally owned and operated street railway. The District Court relied upon the earlier
37 decision in United States *v.* King County, Wash., et al., supra, from which it construed the ownership and operation of the street-railway system by the city of Detroit to be the exer-

cise of a strictly governmental function. The record discloses that the Boston Elevated Railway continued to be owned by the private corporation and that at no time did the Commonwealth of Massachusetts own the railway; thus, in this particular, if in no other, the instant proceedings are distinguishable from those cases relied upon by the petitioners.

Contrasting with the decisions cited by the petitioners, involving ferries and street railways owned and operated by political subdivisions of a State, are the decisions of the District Court, District of Massachusetts, involving the Boston Elevated Railway Company. That court held in Boston Elevated R. Co. v. Malley, 288 Fed. 864 (1923), that the railway was subject to the three percent transportation tax imposed by section 500 of the Revenue Act of October 3, 1917, and in Boston Elevated R. Co. v. Malley 24 Fed. (2d) 758 (1928), that it was subject to the capital-stock tax imposed by section 1000 (a) (1) of the Revenue Act of 1918, while being operated under chapter 159, Special Acts of 1918, by the board of trustees therein provided. In the first case, the court pointed out that the tax was not paid by the Commonwealth of Massachusetts, and in the latter said:

"It should perhaps be noticed that the special act reserved to the Commonwealth and its subdivisions the right 'to tax the company or its stockholders in the same manner and to the same extent as if the company had continued to manage and operate its own property', section 2. It will be a curious arrangement under which the corporation continued to be fully taxable as such for the benefit of the Commonwealth, while it escaped taxation by the Federal Government."

The petitioners further argue that in substance the board of trustees of the Boston Elevated Railway Company constituted a special public service commission for the Boston Elevated Railway and as such they were engaged in an essential governmental function, to wit, regulating the operations of such railway, citing
38 Burnet v. Livezey, 48 Fed. (2d) 159. After the enactment of chapter 159 of Special Acts of 1918 the Public Service Commission of the Commonwealth of Massachusetts continued its functions and duties with respect to public utilities other than the Boston Elevated Railway; thereafter, pursuant to the statute, that railway was operated by the trustees, who at all times acted as "agents of the company and not of the Commonwealth" (section 2, chapter 159, Special Acts of 1918); public regulation abdicated in favor of public operation, and thereafter public regulation was restricted in the manner provided in section 15 of chapter 159, which perhaps was an inducement to the private corporation to subject its property to public operation, during and after which the stockholders of the private corporation were assured a fixed return upon their investment. Burnet v. Livezey, supra, held that an attorney for the Public Service Commission of the State of

West Virginia was employed by an agency of the State performing governmental functions and that his income was exempt from Federal taxation. Here, these petitioners were not members of the Public Service Commission of Massachusetts, nor were they employed by such Commission. The functions of regulation that they exercised were incidental to the public operation. Furthermore, Burnet v. Livezey arose under section 1211 of the Revenue Act of 1926 as applied to the taxable year 1923. Contrast with that decision the holdings in Blair v. Byers, 35 Fed. (2d) 326, and T. P. Wittschen, supra.

In Leon S. Moisseiff, 21 B.T.A. 515, this Board held that the Delaware River Bridge Joint Commission created by legislative enactments of the States of Delaware and Pennsylvania, and the Port of New York Authority, similarly created by legislative enactments of the States of New York and New Jersey, were governmental instrumentalities and that the compensation paid to an employee thereof was exempt from Federal income tax. In that case, the instrumentalities employed by the States concerned were engaged in providing bridge facilities in furtherance of commerce, and making harbor improvements in aid of navigation, and in so
39 doing did not merely take over and operate a private corporation, as in the instant proceedings. In the case of the States of New York and New Jersey, the legislatures thereof expressly provided that the port authority be regarded as performing a governmental function (see page 526); the same inference is drawn from the legislation creating the Delaware River Bridge Joint Commission. Neither enterprise was carried out by the public operation of private property, as in the instant proceedings. Obviously, therefore, that case is not authority for holding tax exempt the income income of these petitioners.*

The record discloses that the compensation of these petitioners as trustees was paid neither directly nor indirectly by the Commonwealth of Massachusetts. The salaries in question were paid by the Boston Elevated Railway Company and it was only in the event of the unsuccessful operation of the railway that the Commonwealth would be called upon to contribute any sum toward the expense of the railway. It appears that over $3,000,000 was advanced by the Commonwealth of Massachusetts in 1919 for this purpose, but that the operations of subsequent years, and particularly the taxable years under consideration, were successful and in some measure the Commonwealth was reimbursed for the amount advanced in 1919. In this particular, the instant proceedings are distinguishable from the situation involved in Biscoe v. Tax Commissioner, 236 Mass. 201, 128 N.E. 16, wherein there was no decision on the question of an essential governmental function, but where the Supreme Court of Massachusetts held that compensation received by a Federal manager and a solicitor of railways, under the supervision of the Director General of Rail-

roads during the period of Federal control, was exempt from the Massachusetts State income tax imposed by chapter 269 of the Statutes of 1916, which in section 5 (b) specifically exempted the salaries of employees and officers of the United States Government. It appears that the moneys out of which the compensation was paid were so handled as to become the moneys of the United States Government and that the taxpayers' compensation was paid by voucher drawn either directly or indirectly upon the Federal Government. The facts in the instant proceedings are vitally different. The test applied by the Massachusetts statute was met in Biscoe v. Tax Commissioner, supra, whereas the test applicable in the instant proceedings has not been met.

From a full consideration of the facts of record in the light of the recent decisions of the Supreme Court, we are of the opinion that the compensation received by these petitioners as trustees of the Boston Elevated Railway Company from the company in the years 1926 to 1929, inclusive, is subject to the Federal income tax asserted by the respondent. These petitioners were engaged in the public operation of private property, as agents of a private corporation, the stockholders of which were assured a fixed return upon their investment during and after public operation, and the railway at all times continued subject to taxation and liable for the acts of its agents. Although public officials, as that term has been liberally interpreted, they were not exercising essential governmental functions in the performance of their duties. The taxation of the compensation in question places no burden upon the Commonwealth of Massachusetts and there is no interference with any essential governmental function of that Commonwealth.

Reviewed by the Board.

Judgments will be entered for the respondent.

Murdock and Goodrich concur in the result.

Before United States Board of Tax Appeals, Washington

Docket No. 47836

LELAND POWERS, EXECUTOR OF THE ESTATE OF SAMUEL L. POWERS, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Decision

Entered October 27, 1932

Pursuant to the determination of the Board, as set forth in its report promulgated October 27, 1932, it is ordered and decided: That there is a deficiency of $553.44 for the year 1927.

CHARLES P. SMITH, *Member.*

41 Before United States Board of Tax Appeals, Washington

Docket No. 51029

WINTHROP COFFIN, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Decision

Entered October 27, 1932

Pursuant to the determination of the Board, as set forth in its report promulgated October 27, 1932, it is ordered and decided: That there is a deficiency of $934.29 for the year 1927.

CHARLES P. SMITH, *Member.*

Before United States Board of Tax Appeals, Washington

Docket No. 61846

HENRY I. HARRIMAN, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Decision

Entered October 27, 1932

Pursuant to the determination of the Board, as set forth in its report promulgated October 27, 1932, it is ordered and decided: That there is a deficiency of $955.66 for the year 1929.

CHARLES P. SMITH, *Member.*

Before United States Board of Tax Appeals

Docket No. 47836

[Title omitted.]

Petition for review

Filed December 22, 1932

The above-named petitioner, Leland Powers, hereby petitions for review of a decision of the United States Board of Tax Appeals rendered upon his appeal numbered in the docket of said Board as above and in support of this his said petition avers as follows:

42 I. The petitioner is an individual residing at 124 Chestnut Hill Road, Newton, in the county of Middlesex and Commonwealth of Massachusetts, and is the duly appointed and qualified executor of the estate of Samuel L. Powers, late of said Newton.

II. The controversy relates to the Federal income tax of the petitioner's decedent for the calendar year 1927. The petitioner claims that the salary received by the petitioner's decedent in the year 1927 as one of the public trustees of the Boston Elevated Railway Company is not subject to the Federal income tax. The Commissioner of Internal Revenue has disallowed this claim, has included said salary in the taxable income of the petitioner's decedent, and in consequence has asserted, and the said Board of Tax Appeals has now by its decision entered October 27, 1932, affirmed, a deficiency for the said year in the sum of $553.44, which decision and deficiency your petitioner asserts to be erroneous.

III. Review of the said decision is sought in the United States Circuit Court of Appeals for the First Circuit.

IV. And the petitioner assigns as errors committed by the said Board in the proceedings and decision aforesaid the following:

(1) The Board erred in its ruling that "the constitutional exemption, if any, must be strictly construed against the taxpayer."

(2) The Board erred in its application to the present case of the authority of Flint v. Stone Tracy Co., 220 U.S. 107, if and insofar as it purported thereby to rule, upon the facts of the present case, that a State is never engaged in the performance of an essential governmental function when dealing with the providing of means of transportation for its inhabitants.

(3) The Board erred in its finding and ruling, upon the evidence, that the functions of regulation exercised by the petitioner's decedent as one of the public trustees were incidental to the public operation of the railway; insofar as the Board thereby, read in conjunction with the remainder of its opinion, purported to rule that the functions of regulation were merely incidental to the functions of operation con-

43 trary to the petitioner's contention that the functions of operation were incidental to and an extension of the functions of regulation for the purpose of rendering the same more effective.

(4) The Board erred in finding and ruling, upon the evidence, that the compensation of the petitioner's decedent as trustee was paid neither directly nor indirectly by the Commonwealth of Massachusetts.

(5) The Board erred in ruling, if and insofar as it did so rule, that the fact if true that the compensation of the petitioner's decedent as trustee was paid neither directly nor indirectly by the Commonwealth of Massachusetts was decisive against the petitioner's case.

(6) The Board erred in finding and ruling, upon the evidence, that the compensation received by the petitioner's decedent as

trustee of the Boston Elevated Railway for the year 1927 was subject to the Federal income tax asserted by the respondent.

(7) The Board erred in finding and ruling, upon the evidence, that the petitioner's decedent although a public official was not exercising essential governmental functions in the performance of his duties.

(8) The Board erred in finding and ruling, upon the evidence, that the taxation of the compensation in question places no burden upon the Commonwealth of Massachusetts.

(9) The Board erred in finding and ruling, upon the evidence, that "there is no interference with any essential governmental function of that Commonwealth."

Wherefore the petitioner prays that the said decision may be reviewed by the said United States Circuit Court of Appeals for the First Circuit and be reversed and the said deficiency disallowed.

LELAND POWERS,
Executor of the Estate of Samuel L. Powers.

[*Duly sworn to by Leland Powers, jurat omitted in printing.*]

44 Before United States Board of Tax Appeals

Docket No. 47836

[Title omitted.]

Affidavit of service of petition for review

Filed January 20, 1933

Melville F. Weston, of lawful age, having been first duly sworn, upon his oath states:

That he served the petition for review in the above-entitled case and notice of filing the same on the Commissioner of Internal Revenue by sending a copy of said petition with a letter of notification of which the attached is a correct copy by registered United States mail to C. M. Charest, Esq., general counsel, Bureau of Internal Revenue at Washington, D.C.; that said copy and letter were enclosed in an envelope bearing the return address of Powers & Hall, 30 Federal Street, Boston, Massachusetts, and properly addressed to said C. M. Charest, Esq., as aforesaid; that said copy and letter so registered were deposited in the United States mail on January 6, 1933.

MELVILLE F. WESTON,

COMMONWEALTH OF MASSACHUSETTS,
Suffolk, ss:

BOSTON, *January 18, 1933.*

Subscribed and sworn to, before me,
[SEAL]

MATT B. JONES, JR.,
Notary Public.

Before United States Board of Tax Appeals

Docket No. 51029

[Title omitted.]

Petition for review

Filed December 22, 1932

The above-named petitioner, Winthrop Coffin, hereby petitions for review of a decision of the United States Board of Tax
45 Appeals rendered upon his appeal numbered in the docket of said Board as above and in support of this his said petition avers as follows:

I. The petitioner is an individual residing at 45 Warren Street, Brookline, in the county of Norfolk and Commonwealth of Massachusetts.

II. The controversy relates to the Federal income tax of the petitioner for the calendar year 1927. The petitioner claims that the salary received by him in the year 1927 as one of the public trustees of the Boston Elevated Railway Company is not subject to the Federal income tax. The Commissioner of Internal Revenue has disallowed this claim, has included said salary in the petitioner's taxable income, and in consequence has asserted, and the said Board of Tax Appeals has now by its decision entered October 27, 1932, affirmed, a deficiency for the said year in the sum of $934.29, which decision and deficiency your petitioner asserts to be erroneous.

[Memorandum. The remaining paragraphs III to IV (9), being the same as those in no. 47836, printed at pages 42 and 43, are here omitted. A. I. Charron, clerk.]

Wherefore the petitioner prays that the said decision may be reviewed by the said United States Circuit Court of Appeals for the First Circuit and be reversed and the said deficiency disallowed.

WINTHROP COFFIN.

[*Duly sworn to by Winthrop Coffin, jurat omitted in printing.*]

46 Before United States Board of Tax Appeals

Docket No. 51029

[Title omitted.]

Affidavit of service of petition for review

Filed January 20, 1933

[Memorandum. The affidavit of service, being the same as that in no. 47836, already printed at page 44, is here omitted. A. I. Charron, clerk.]

Before United States Board of Tax Appeals

Docket No. 61846

[Title omitted.]

Petition for review

Filed December 22, 1932

The above-named petitioner, Henry I. Harriman, hereby petitions for review of a decision of the United States Board of Tax Appeals rendered upon his appeal numbered in the docket of said Board as above and in support of this his said petition avers as follows:

I. The petitioner is an individual residing at 825 Centre Street, Newton, in the county of Middlesex and Commonwealth of Massachusetts.

II. The controversy relates to the Federal income tax of the petitioner for the calendar year 1929. The petitioner claims that the salary received by him in the year 1929 as one of the public trustees of the Boston Elevated Railway Company is not subject to the Federal income tax. The Commissioner of Internal Revenue has disallowed this claim, has included said salary in the petitioner's taxable income, and in consequence has asserted, and the said Board of Tax Appeals has now by its decision entered October 27, 1932,
47 affirmed, a deficiency for the said year in the sum of $955.66, which decision and deficiency your petitioner asserts to be erroneous.

[Memorandum. The remaining paragraphs, III to IV (9), being the same as those in no. 47836, already printed as pages 42 and 43, are here omitted. A. I. Charron, clerk.]

Wherefore the petitioner prays that the said decision may be reviewed by the said United States Circuit Court of Appeals for the First Circuit and be reversed and the said deficiency disallowed.

HENRY I. HARRIMAN.

[*Duly sworn to by Henry I. Harriman, jurat omitted in printing.*]

Before United States Board of Tax Appeals

Docket No. 61846

[Title omitted.]

Affidavit of service of petition for review

Filed January 20, 1933

[Memorandum. The affidavit of service being the same as that in no. 47836, already printed at page 44, is here omitted. A. I. Charron, clerk.]

48 Before United States Board of Tax Appeals

Docket No. 47836

[Title omitted.]

Statement of the evidence

Lodged December 22, 1932. Filed January 20, 1933

The above-entitled appeal was consolidated for hearing and decision with four other pending cases (Stanley R. Miller, no. 48007; Stanley R. Miller, no. 50575; Henry I. Harriman, no. 61846; Winthrop Coffin, no. 51029). The evidence consisted of stipulations of facts severally entered into by each petitioner and the respondent. The stipulation which constituted the entire evidence upon the above-entitled appeal was as follows:

It is hereby stipulated and agreed by and between the parties in the case entitled and numbered as above that the following facts are true:

1. All facts alleged in the petition and admitted by the answer of the respondent thereto.

2. The office of trustee of the Boston Elevated Railway Company was created by chapter 159 of the Special Acts of 1918 of the Commonwealth of Massachusetts, which act was passed in May 1918 and went into full force and effect in that year, all prescribed conditions, as to acceptance by stockholders and the like, having been fulfilled. Said act was in force and effect throughout the year 1927. For the general background in fact of this legislation, reference may be made to the various decisions and opinions of the Supreme Judicial Court of Massachusetts and the United States Supreme Court wherein the same is discussed, cited in the decision of the Board in the case of Winthrop Coffin v. Commissioner of Internal Revenue, 12 B.T.A. 703.

3. The petitioner's decedent was duly qualified for appointment to the office of member of the Board of Trustees of the Boston Elevated Railway Company. As required by section 1 of said act,
49 he did not own any stock or other securities of the Boston Elevated Railroad Company or of any company owned, leased, or operated by it.

4. If material, the Commonwealth in the year 1919 became required, under the terms of said act, and especially section 11 thereof, to pay over to the board of trustees of the Boston Elevated Railway Company the sum of $3,980,151.67. This amount was determined by the board of trustees of the Boston Elevated Railway Company and by them apportioned among the cities and towns in which the railway was operated. No reimbursements were made to the Commonwealth on account of said payment prior to 1922 nor in the year 1924. Operations during the years down to and including 1928 did not result in an excess sufficient to enable the full reimbursement of the $3,980,151.67 to the Commonwealth.

5. The deficiency in tax involved in the petition arises wholly from the inclusion by the Commissioner of the salary of the petitioner's decedent as one of the trustees of the Boston Elevated Railway Company for the year in question.

6. The tax return of the petitioner's decedent for the year in question may be placed in evidence. The said chapter 159 of the Special Acts of 1918 of the Commonwealth of Massachusetts may be judicially noticed, and as well any other pertinent provision of Massachusetts or United States law.

MELVILLE F. WESTON,
Attorney for Petitioner.

C. M. CHAREST,
Attorney for Respondent.

Agreed to January 19, 1933.

C. M. CHAREST,
Attorney for Petitioner.

Approved and ordered filed this twentieth day of January 1933.
CHARLES P. SMITH, *Member.*

[Memorandum. By stipulation and agreement between the parties the statements of the evidence in the cases of Winthrop Coffin, B.T.A. no. 51029, and Henry I. Harriman, B.T.A. no. 61846, being in all material respects identical with the statement of the evidence in the case of Leland Powers, executor, B.T.A. no. 47836, the same are omitted in the printing of the record.]

50

Before United States Board of Tax Appeals

[Titles omitted.]

Docket No. 51029

Docket No. 61846

Docket No. 47836

Praecipe for transcript of record

Filed January 19, 1933

To the Clerk of the United States Board of Tax Appeals:

Will you please prepare at the petitioners' expense and transmit forthwith to the clerk of the United States Circuit Court of Appeals for the First Circuit a transcript of the record in the causes entitled and numbered as above, including therein the following papers and proceedings, namely:

1. The docket entries of the proceedings before the United States Board of Tax Appeals in the said causes.

2. The pleadings before the Board.
3. The findings of fact and opinion of the Board.
4. The decision of the Board entered upon each of said appeals pursuant to the said findings of fact and opinion.
5. The petitions for review including affidavit of service of petition for review.
6. The statement of the evidence.
7. This praecipe.

The foregoing to be prepared, certified, and transmitted as
51 required by law and the rules of the United States Circuit Court of Appeals for the First Circuit.

MELVILLE F. WESTON,
Attorney for Petitioners,
30 Federal Street, Boston, Massachusetts.

January 18, 1933.

Service of a copy of the foregoing is hereby acknowledged this nineteenth day of January 1933.

C. M. CHAREST,
Attorney for Respondent.

[Clerk's certificate to foregoing transcript omitted in printing.]

52 Before United States Board of Tax Appeals

Docket no. 48007

STANLEY R. MILLER, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Appearances:
For taxpayer: Stanley R. Miller, Esq.
For Commissioner: Harold Allen, Esq.

Docket entries

1930

Mar. 28—Petition received and filed. Taxpayer notified. (Fee paid.)
" 29—Copy of petition served on general counsel.
Apr. 26—Answer filed by general counsel.
May 9—Copy of answer served on taxpayer. General Calendar.

1931

Feb. 11—Motion to consolidate with dockets 51029 and 47836 filed by taxpayer.
" 14—Motion granted.

[Memorandum.—The remaining docket entries, February 11, 1932, to February 19, 1933, being practically the same as those printed in no. 47836 at pages 1 and 2, are here omitted. A. I. Charron, clerk.]

53 Before United States Board of Tax Appeals

Docket No. 50575

STANLEY R. MILLER, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Appearances:

For taxpayer: Melville F. Weston, Esq., Robert H. Montgomery, Esq.

For Commissioner: Harold Allen, Esq.

Docket entries

1930
Nov. 1—Petition received and filed. Taxpayer notified. (Fee paid.)
" 3—Copy of petition served on general counsel.
Dec. 22—Answer filed by general counsel.
1931
Jan. 14—Copy of answer served on taxpayer. General calendar.
Feb. 11—Motion to consolidate with dockets 51029, 47836, and 48007 filed by taxpayer.
" 14—Motion granted.

[Memorandum. The remaining docket entries, February 11, 1932, to February 19, 1933, being practically the same as those printed in no. 47836 at pages 1 and 2, are here omitted. A. I. Charron, clerk.]

54 Before United States Board of Tax Appeals

Docket No. 48007

[Title omitted.]

Petition

Filed March 28, 1930

The above-named petitioner hereby petitions for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his notice of deficiency symbolized IT: AR: B-12 JMF-60D dated February 13, 1930, and as a basis of his proceeding alleges as follows:

1. The petitioner is an individual residing at 1258 Beacon Street, Brookline, Massachusetts (formerly residing at 280 Dudley Street in said Brookline).

2. The notice of deficiency (a copy of which is attached and marked "Exhibit A") was mailed to the petitioner on February 13, 1930.

3. The taxes in controversy are income taxes for the years 1926 and 1927, and for five hundred seventy-five and 25/100 dollars ($575.25), the entire amount of said alleged deficiency.

4. The Commissioner has held that the salary, amounting to five thousand dollars ($5,000), received by the petitioner as a member of the board of trustees of the Boston Elevated Railway Company for and during each of the years 1926 and 1927 under the provisions of chapter 159 of the Special Acts of the General Court of Massachusetts for the year 1918, is subject to an income tax imposed by the Revenue Act of 1926 because said salary received by the petitioner as an officer of the Commonwealth of Massachusetts "was not derived from the exercise of any essential governmental function as provided by section 213 (c) (7) of the Revenue Act of 1926, and article 88, Regulations 69." Said determination of tax as set forth in the said notice of deficiency is based upon the following errors:

55 (a) The determination that the petitioner did not receive said salary from the exercise of any essential governmental function.

(b) The requirement that said salary of said petitioner must have been received for services rendered in connection with the exercise of an essential governmental function of the Commonwealth of Massachusetts in order to be exempt from taxation.

(c) The ruling that section 213 (c) (7) of the Revenue Act of 1926 (even assuming 213 (b) (7) is intended to be referred to) provides for or justifies the inclusion of said salary in gross income.

5. The facts upon which the petitioner relies as the basis of this proceeding are as follows:

On June 26, 1918, the petitioner was appointed by the Governor of the Commonwealth of Massachusetts, with the advice and consent of the executive council, a member of the board of trustees of the Boston Elevated Railway Company under the provisions of chapter 159 of the Special Acts of the General Court of said Commonwealth for 1918, entitled "An act to provide for the public operation of the Boston Elevated Railway Company", for a term of office expiring July 1, 1928, and thereupon qualified for said office by taking the oaths required by the Constitution and laws of the Commonwealth of Massachusetts to be taken by public officials before entering upon the discharge of their duties. On the foregoing facts this Board held in the petitioner's case, docket no. 17002, promulgated June 19, 1926, that the petitioner was an officer of the Commonwealth of Massachusetts.

Acting under the provisions of said act, the board of trustees did assume the management and operation of the properties of the Boston Elevated Railway Company on July 1, 1918, and since that date and during the taxable years in question had possession of said properties in behalf of the Commonwealth.

During each of the years 1926 and 1927, by virtue of said appointment and qualification, the petitioner acted as said trustee and officer of the Commonwealth of Massachusetts and received as salary therefor the sum of five thousand dollars ($5,000), pursuant to the terms of said act.

The act above referred to transferred to the board of trustees
56 powers of management and operation previously vested in the board of directors of the private corporation. The powers thus transferred include the right to make contracts in the name of the corporation; to receive and pay out all income or other moneys to which it is entitled; to issue stock, bonds, or promissory notes of the company; and to appoint and remove all officers of the company other than the board of directors.

Under said act the trustees are also given the right to regulate and fix fares, including the issue, granting, and withdrawal of transfers, and the imposition of charges therefor, and to determine the character and extent of the service and facilities to be furnished and "in these respects their authority shall be exclusive and shall not be subject to the approval, control, or direction of any other State board or commission." Powers were thus given the board of trustees which had been previously vested in and exercised by the Public Service Commission of the Commonwealth of Massachusetts, and by virtue of said chapter 159 said board of trustees became at all times after July 1, 1918, a special public service commission in respect to the Boston Elevated Railway Company.

A more extended statement of the separate provisions of said chapter 159 is here omitted in view of the former decision of this Board in the case docket no. 17002 between the same parties, but said chapter 159 which became effective in all its provisions. is hereby attached, marked "Exhibit B", and made a part hereof.

6. Therefore the petitioner says that in exercising the powers given to, and performing the duties placed upon, the petitioner, as one of said board of trustees, he was a public officer of the Commonwealth of Massachusetts, that he was discharging the duties of an office which involved the exercise of an essential governmental function, that as said officer he received the salary on which the Commissioner has determined said deficiency tax is due and that whatever compensation he received is not taxable under said Revenue Act of 1926; and the petitioner prays for relief from the deficiency asserted by the respondent on the following particulars:

57 (a) The entire amount of deficiency as determined by the Commissioner as above set forth.

Wherefore, the petitioner prays that this Board may hear and disallow the deficiency determined by the Commissioner as above set forth.

STANLEY R. MILLER,
Petitioner, 31 Milk Street, Boston, Massachusetts.

[*Duly sworn to by Stanley R. Miller, jurat omitted in printing.*]

Exhibit A to petition

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington, February 13, 1930.

Mr. STANLEY R. MILLER,
280 Dudley Street, Brookline, Massachusetts.

SIR: In accordance with section 274 of the Revenue Act of 1926, you are advised that the determination of your tax liability for the years 1926 and 1927 discloses a deficiency of $575.25, as shown in the statement attached.

The section of the law above mentioned allows you to petition the United States Board of Tax Appeals within sixty days (not counting Sunday as the sixtieth day) from the date of the mailing of this letter for a redetermination of your tax liability.

However, if you do not desire to petition, you are requested to execute the inclosed Form 866 and forward both original and
58 duplicate to the Commissioner of Internal Revenue, Washington, D.C., for the attention of IT:C:P-7. The signing of this agreement form will expedite the closing of your return by permitting an early assessment of any deficiencies and preventing the accumulation of interest charges, since the interest period terminates thirty days after filing the agreement form, or on the date assessment is made, whichever is earlier; whereas if no agreement is filed, interest will accumulate to the date of assessment of the deficiencies.

Respectfully,

ROBT. H. LUCAS,
Commissioner.
By DAVID BURNET,
Deputy Commissioner.

Inclosures: Statement. Form 866. Form 882.

STATEMENT

IT:AR:B-12. JMF-60D. FEBRUARY 13, 1930.

In re: Mr. Stanley R. Miller, 280 Dudley Street, Brookline, Massachusetts

Tax liability

Year	Corrected tax liability	Tax previously assessed	Deficiency
1926	$373.50	$132.61	$240.89
1927	608.77	274.41	334.36
Totals	$982.27	$407.02	$575.25

Information on file in this office discloses that for each of the years under consideration you received a salary of $5,000.00 as one of five trustees for the State of Massachusetts of the Boston Elevated Railway Company, which amount was not reported in your returns.

1926

Total net income reported	$12,032.13
Add: Salary from Boston Elevated Railway Co	5,000.00
Net income adjusted	$17,032.13

The amount of $5,000.00 has been added to income reported
59 for the reason it is held that the salary was not derived from the exercise of any essential governmental function as provided by section 213 (c) (7) of the Revenue Act of 1926, and article 88, Regulations 69. You are informed that to be entitled to the exemption provided by the Revenue Act of 1926 the services must have been rendered in connection with the exercise of an essential governmental function of the state or political subdivision. In this connection your attention is called to General Counsel Memorandum #3142, published in Cumulative Bulletin VII–1 at page 78.

COMPUTATION OF EARNED INCOME CREDIT

Earned in come reported	$12,859.79
Salary	5,000.00
Total earned income	$17,859.79
Less: Personal exemption	4,700.00
Balance subject to normal tax	$13,159.79
Normal tax at 1½% on $4,000.00	$60.00
Normal tax at 3% on $4,000.00	120.00
Normal tax at 5% on $5,159.79	257.99
Surtax on $17,859.79	135.79
Total	$573.78
25% of $573.78	143.44

Under the provisions of section 209 (b) of the Revenue Act of 1926 the earned income credit is limited to 25% of the normal tax plus 25% of the surtax on earned income, or $132.94, computed as follows:

Normal tax	$395.98
Surtax on earned income	135.79
Total	531.77
Earned income credit of 25%	132.94

60 COMPUTATION OF TAX

Net income adjusted		17,032.13
Less:		
Dividends	$12.50	
Personal exemption	4,700.00	
		4,712.50
Balance subject to normal tax		12,319.63

COMPUTATION OF TAX—Continued

Normal tax at 1½% on $4,000.00		$60.00
Normal tax at 3% on $4,000.00		120.00
Normal tax at 5% on $4,319.63		215.98
Surtax on $17,032.13		110.96
Total		$506.94
Less:		
Earned income credit	$132.94	
Income tax paid at source	.50	
		133.44
Tax liability		$373.50
Previously assessed		132.61
Deficiency		$240.89

1927

Total net income reported	$15,410.20
Add: Salary from Boston Elevated Railway Company	5,000.00
Net income adjusted	$20,410.20

The amount of $5,000.00 salary has been added to income reported for the same reason fully explained above for the year 1926.

COMPUTATION OF EARNED INCOME CREDIT

Earned income reported	$16,589.89
Salary	5,000.00
Total earned income	21,589.89
Earned income limited by section 209 (b) of the Revenue Act of 1926	20,000.00
Less: Personal exemption	4,700.00
Balance subject to normal tax	15,300.00
61 Normal tax at 1½% on $4,000.00	$60.00
Normal tax at 3% on $4,000.00	120.00
Normal tax at 5% on $7,300.00	365.00
Surtax on $20,000.00	220.00
Total	765.00
Earned income credit of 25%	191.25

COMPUTATION OF TAX

Net income adjusted	20,410.20
Less: Personal exemption	4,700.00
Balance subject to normal tax	15,710.20
Normal tax at 1½% on $4,000.00	60.00
Normal tax at 3% on $4,000.00	120.00
Normal tax at 5% on $7,710.20	385.51
Surtax on $20,410.20	240.51
Total	806.02
Less:	
Earned income credit	$191.25
Income tax paid at source	6.00
	197.25
Tax liability	608.77
Tax previously assessed	274.41
Deficiency	334.36

Payment should not be made until a bill is received from the Collector of Internal Revenue for your district, and remittance should then be made to him.

Exhibit B

CHAPTER 159, SPECIAL ACTS, 1918

[Memorandum. Omitted by direction of counsel. A. I. Charron, clerk.]

62 Before United States Board of Tax Appeals

Docket No. 48007

[Title omitted.]

Answer

Filed April 26, 1930

The Commissioner of Internal Revenue, by his attorney, C. M. Charest, General Counsel, Bureau of Internal Revenue, for answer to the petition filed by above-named taxpayer, admits and denies as follows:

1. Admits the averments contained in paragraph 1.
2. Admits the averments contained in paragraph 2.
3. Admits the averments contained in paragraph 3.
4. Denies error in the action stated in paragraph 4.
5. Admits the averments contained in paragraph 5.
6. Admits the averments contained in paragraph 6 with the exception of the averment that petitioner's compensation is not taxable under the Revenue Act of 1926, which averment is denied.

Wherefore, it is prayed that the taxpayer's petition be denied.

[SEAL] C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

Of counsel:
HAROLD ALLEN,
Special Attorney, Bureau of Internal Revenue.

Before United States Board of Tax Appeals

[Title omitted.]

Docket 48007

Amended answer

Filed August 26, 1932

The Commissioner of Internal Revenue, by his attorney, C. M. Charest, General Counsel, Bureau of Internal Revenue, for amended

answer to the petition filed by above-named taxpayer, admits and denies as follows:

1. Admits the averments contained in paragraph 1.
2. Admits the averments contained in paragraph 2.
3. Admits the averments contained in paragraph 3.
4. Denies error in the action stated in paragraph 4.
5. Admits the averments contained in paragraph 5.
6. Admits the averments contained in paragraph 6 with the
63 exception of the averment that petitioner's compensation is not taxable under the Revenue Act of 1926, and the averment that petitioner was discharging the duties of an office which involved the exercise of an essential governmental function, which averments are denied.

Wherefore, it is prayed that the taxpayer's petition be denied.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

Of counsel:
HAROLD ALLEN,
Special Attorney, Bureau of Internal Revenue.

Before United States Board of Tax Appeals

Docket no. 50575

[Title omitted.]

Petition

Filed November 1, 1930

The above-named petitioner hereby petitions for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his notice of deficiency symbolized IT:AB:B–1 DAC–60D dated September 26, 1930, and as a basis of his proceeding alleges as follows:

1. The petitioner is an individual residing at 1258 Beacon Street, Brookline, Massachusetts, and having a regular and usual place of business at 31 Milk Street, Boston, Massachusetts.

2. The notice of deficiency (a copy of which is attached and marked "Exhibit A") was mailed to petitioner on September 26, 1930.

3. The tax in controversy is an income tax for the year 1928 and for two hundred twenty-six and 92/100 dollars ($226.92), the entire amount of said alleged deficiency.

4. The Commissioner has held that the salary, amounting to five thousand dollars ($5,000), received by the petitioner as a
64 member of the board of trustees of the Boston Elevated Railway Company for and during the calendar year 1928 under the provisions of chapter 159 of Special Acts of the General Court of Massachusetts for the year 1918 is subject to an income tax imposed by the Revenue Act of 1926 and amendments thereto because

said salary received by the petitioner as an officer of the Commonwealth of Massachusetts " was not derived from the exercise of an essential governmental function as provided by article 643 of Regulations 74."

Said determination of tax as set forth in the said notice of deficiency is based upon the following errors:

(a) The determination that the petitioner did not receive said salary from the exercise of any essential governmental function.

(b) The requirement that said salary of said petitioner must have been received for services rendered in connection with the exercise of an essential governmental function of the Commonwealth of Massachusetts in order to be exempt from taxation.

5. The facts upon which the petitioner relies as the basis of this proceeding are as follows:

On June 26, 1918, the petitioner was appointed by the Governor of the Commonwealth of Massachusetts, with the advice and consent of the executive council, a member of the board of trustees of the Boston Elevated Railway Company under the provisions of chapter 159 of the Special Acts of the General Court of said Commonwealth for 1918, entitled "An act to provide for the public operation of the Boston Elevated Railway Company ", for a term of office extending until July 1, 1928, and thereafter until a successor should be appointed and qualified and thereupon the petitioner qualified for said office by taking the oaths required by the Constitution and laws of the Commonwealth of Massachusetts to be taken by public officials before entering upon the discharge of their duties. On the foregoing facts this Board held in the petitioner's case Docket Number 17002, promulgated June 19, 1926, that the petitioner was an officer of the Commonwealth of Massachusetts. On December 26, 1928, the petitioner was reappointed by the Governor of the Commonwealth
65 of Massachusetts, with the advice and consent of the executive council, a member of the board of trustees of said Boston Elevated Railway Company under the provisions of said chapter 159 for a further term of ten years from July 1, 1928, and he thereupon qualified for said office on December 27, 1928, by taking the oaths required by the Constitution and laws of the Commonwealth of Massachusetts to be taken by public officials before entering upon the discharge of their duties and thereby the petitioner continued (an officer of the Commonwealth of Massachusetts throughout the calendar year 1928).

Acting under the provisions of said act the board of trustees did assume the management and operation of the properties of the Boston Elevated Railway Company on July 1, 1918 and since that date and during the taxable year in question had possession of said properties in behalf of the Commonwealth.

During the year 1928 by virtue of said appointments and qualifications the petitioner acted as said trustee and officer of the Com-

monwealth of Massachusetts and received as salary therefor the sum of five thousand dollars ($5,000) pursuant to the terms of said act.

[Memorandum. The remainder of this petition being the same as the petition in no. 48007, printed at pages 55 to 57, inclusive, is here omitted. A. I. Charron, clerk.]

Wherefore, the petitioner prays that this Board may hear and disallow the deficiency determined by the Commissioner as above set forth.

STANLEY R. MILLER,
Petitioner, 31 Milk Street, Boston, Massachusetts.

[*Duly sworn to by Stanley R. Miller, jurat omitted in printing.*]

66 *Exhibit A to petition*

TREASURY DEPARTMENT,
Washington, September 26, 1930.

Mr. STANLEY R. MILLER,
31 Milk Street, Boston, Massachusetts.

SIR: You are advised that the determination of your tax liability for the year 1928 discloses a deficiency of $226.92 as shown in the statement attached.

In accordance with section 272 of the Revenue Act of 1928, notice is hereby given of the deficiency mentioned. Within sixty days (not counting Sunday as the sixtieth day) from the date of the mailing of this letter, you may petition the United States Board of Tax Appeals for a redetermination of your tax liability.

However, if you do not desire to petition, you are requested to execute the enclosed agreement form and forward it to the Commissioner of Internal Revenue, Washington, D.C., for the attention of IT:C:P–7. The signing of this agreement will expedite the closing of your return by permitting an early assessment of any deficiency and preventing the accumulation of interest charges, since the interest paid terminates thirty days after filing the enclosed agreement, or on the date assessment is made, whichever is earlier; whereas if no agreement is filed, interest will accumulate to the date of assessment of the deficiency.

Respectfully,

DAVID BURNET,
Commissioner.
By J. C. WILMER,
Deputy Commissioner.

Enclosures: Statement. Form 882. Form 870.

67 STATEMENT

IT:AR:B-1. DAC-60D.

In re: Mr. Stanley R. Miller, 31 Milk Street, Boston, Massachusetts

Tax liability

Year	Corrected tax liability	Tax previously assessed	Deficiency
1928	$354.44	$127.52	$226.92

The report of the internal revenue agent in charge at Boston, Massachusetts, covering your income tax liability for the year 1928 has been reviewed and approved as submitted. The report shows the following adjustment:

	1928
Net income reported on your return	$12,340.44
Add: 1. Salary from Boston Elevated Railway Co	5,000.00
Net income adjusted	17,340.44
COMPUTATION OF TAX	
Net income subject to surtax	17,340.44
Less: Personal exemption and credit for dependents	4,300.00
Balance subject to normal tax	13,040.44
Normal tax at 1½% on $4,000.00	60.00
Normal tax at 3% on $4,000.00	120.00
Normal tax at 5% on $5,040.44	252.02
Surtax on $17,340.44	120.21
Total	552.23
Less: Credit of 25% of the tax on earned net income	197.79
Total tax assessable	354.44
Tax previously assessed	127.52
Deficiency	226.92
COMPUTATION OF EARNED INCOME CREDIT	
Earned net income reported	17,652.30
Add: Salary	5,000.00
Earned net income adjusted	22,652.30
68 Earned net income subject to tax	22,652.30
Less: Personal exemption and credit for dependents	4,300.00
Balance	18,352.30
Normal tax at 1½% on $4,000.00	60.00
Normal tax at 3% on $4,000.00	120.00
Normal tax at 5% on $10,352.30	517.61
Surtax on $22,652.30	359.14
Total	1,056.75
Credit: 25% (not over 25% of items 28, 42, 43, and 44) credit limited to $197.79	264.19

EXPLANATION OF CHANGE

1. Salary of $5,000.00 received by you as compensation for services as trustee of the Boston Elevated Railway Company has been added to income.

The Bureau holds that salary received by the trustees of the Boston Elevated Railway Company was not derived from the exercise of an essential, governmental function as provided by article 643 of Regulations 74, and hence such income should be included for taxation.

Payment should not be made until a bill is received from the collector of internal revenue for your district, and remittance should then be made to him.

Exhibit B

CHAPTER 159, SPECIAL ACTS, 1918

[Memorandum. Omitted by direction of counsel. A. I. Charron, clerk.]

69 Before United States Board of Tax Appeals

Docket No. 50575

[Title omitted.]

Answer

Filed December 22, 1930

The Commissioner of Internal Revenue, by his attorney, C. M. Charest, general counsel, Bureau of Internal Revenue, for answer to the petition filed by above-named taxpayer, admits and denies as follows:

1. Admits the averments contained in paragraph 1.
2. Admits the averments contained in paragraph 2.
3. Admits the averments contained in paragraph 3.
4. Denies error in the action complained of in paragraph 4.
5. Admits the averments contained in paragraph 5, with the exception that the petitioner was an officer of the Commonwealth of Massachusetts, which averment is denied.
6. Denies the averments contained in paragraph 6.

Wherefore, it is prayed that the taxpayer's petition be denied.

C. M. CHAREST,

[SEAL] *General Counsel, Bureau of Internal Revenue.*

Of counsel:

HAROLD ALLEN,

Special Attorney, Bureau of Internal Revenue.

Findings of Fact and Opinion

[Memorandum. Already printed at pages 23 to 40, inclusive. Findings of Fact and Opinion are here omitted. A. I. Charron, clerk.]

70 Before United States Board of Tax Appeals, Washington

Docket No. 48007

STANLEY R. MILLER, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Decision

Entered October 27, 1932

Pursuant to the determination of the Board, as set forth in its report promulgated October 27, 1932, it is

Ordered and decided: That there are deficiencies of $240.89 and $334.36 for the years 1926 and 1927, respectively.

CHARLES P. SMITH, MEMBER

Before United States Board of Tax Appeals, Washington

Docket No. 50575

STANLEY R. MILLER, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Decision

Entered October 27, 1932

Pursuant to the detremination of the Board, as set forth in its report promulgated October 27, 1932, it is

Ordered and decided: That there is a deficiency of $226.92 for the year 1928.

CHARLES P. SMITH, *Member.*

Before United States Board of Tax Appeals

Docket No. 48007

[Title omitted.]

Petition for Review

Filed December 22, 1932

The above-named petitioner, Stanley R. Miller, hereby petitions for review of a decision of the United States Board of Tax
71 Appeals rendered upon his appeal numbered in the docket of said Board as above and in support of this his said petition avers as follows:

I. The petitioner is an individual residing at 94 Centre Street, Milton, in the county of Norfolk and Commonwealth of Massachusetts (formerly residing at 280 Dudley Street, Brookline).

II. The controversy relates to the Federal income taxes of the petitioner for the calendar years 1926 and 1927. The petitioner claims that the salary in the years 1926 and 1927 as one of the public trustees of the Boston Elevated Railway Company is not subject to the Federal income tax. The Commissioner of Internal Revenue has disallowed this claim, has included said salary in the petitioners' taxable income, and in consequence has asserted, and the said Board of Tax Appeals has now by its decision entered October 27, 1932, affirmed, a deficiency for the said years in the sum of $575.25, which decision and deficiency your petitioner asserts to be erroneous.

(Memorandum. The remaining paragraphs III to IV (9) being the same as those in no. 47836 except that the word "petitioner" is substituted for the words "petitioner's decedent", printed at pages 42 and 43, are here omitted. A. I. Charron, clerk.)

Wherefore, the petitioner prays that the said decision may be reviewed by the said United States Circuit Court of Appeals for the First Circuit and be reversed and the said deficiency disallowed.

STANLEY R. MILLER.

[*Duly sworn to by Stanley R. Miller; jurat omitted in printing.*]

72 Before United States Board of Tax Appeals

Docket No. 48007

[Title omitted.]

Affidavit of service of petition for review

Filed January 20, 1933

Stanley R. Miller, of lawful age, having been first duly sworn, upon his oath states:

That he served the petition for review in the above-entitled case and notice of filing the same on the Commissioner of Internal Revenue by sending a copy of said petition with a letter of notification of which the attached is a correct copy by registered United States mail to C. M. Charest, Esq., general counsel, Bureau of Internal Revenue, at Washington, D.C.; that said copy and letter were enclosed in an envelope bearing the return address of Stanley R. Miller, 31 Milk Street, Boston, Massachusetts, and properly addressed to said C. M. Charest, Esq., as aforesaid; that said copy and letter so registered were deposited in the United States mail on January 9, 1933.

STANLEY R. MILLER.

BOSTON, *January 9, 1933.*

COMMONWEALTH OF MASSACHUSETTS,
Suffolk, ss:

Subscribed and sworn to before me.

[SEAL] RANSOM C. PINGREE,
Notary Public.

Before United States Board of Tax Appeals

Docket No. 50575

[Title omitted.]

Petition for review

Filed December 22, 1932.

(Memorandum. This petition for review being the same as the petition for review in no. 48007, except that taxes here involved are for the calendar year 1928 instead of the years 1926 and 1927, printed at pages 70 and 71, is here omitted. A. I. Charron, clerk.)

73 Before United States Board of Tax Appeals

Docket no. 50575

[Title omitted.]

Affidavit of service of petition for review

Filed January 20, 1933

[Memorandum. Being identical with the affidavit of service in no. 48007, printed at page 72, this affidavit of service is here omitted. A. I. Charron, clerk.]

Before United States Board of Tax Appeals

Docket no. 48007

[Title omitted.]

Statement of the evidence

Filed January 20, 1933

The above-entitled appeal was consolidated for hearing and decision with four other pending cases (Leland Powers, executor, no. 47836; Henry I. Harriman, no. 61846; Stanley R. Miller, no. 50575; Winthrop Coffin, no. 51029). The evidence consisted of stipulations of facts severally entered into by each petitioner and the respondent. The stipulation which constituted the entire evidence upon the above-entitled appeal was as follows:

It is hereby stipulated and agreed by and between the parties hereto as follows:

The petitioner is an individual residing at Brookline, Mass. The notice of deficiency (a copy of which is attached to the petition in this case, marked "Exhibit A") was mailed to the petitioner on February 13, 1930. This petition, Docket No. 48007, was filed with the Board of Tax Appeals, March 28, 1930. The taxes in controversy are income taxes for the years 1926 and 1927, the entire amount of said alleged deficiency being five hundred seventy-five dollars and twenty-five cents ($575.25) as set forth in said exhibit A.

On June 26, 1918, the petitioner was appointed by the Governor of the Commonwealth of Massachusetts, with the advice and consent of the executive council, a member of board of trustees of
74 the Boston Elevated Railway Company, pursuant to the provisions of chapter 159 of the Special Acts of said Commonwealth for 1918, for a term of office expiring July 1, 1928, and the petitioner, owning no stock or other securities of the Boston Elevated Railway Company or of any company owned, leased, or operated by it, thereupon qualified for said office by taking the oaths required by the constitution and the laws of the Commonwealth of Massachusetts to be taken by public officials before entering upon the discharge of their duties.

In 1926 and 1927 the petitioner, as a trustee of the Boston Elevated Railway Company, was an officer of the Commonwealth of Massachusetts, and by virtue of holding said office received as compensation therefor in each year the sum of five thousand dollars ($5,000) as provided in said chapter 159 of the Special Acts of 1918.

The Commissioner has held that this salary amounting to five thousand dollars ($5,000) received by the petitioner as a member of the board of trustees of the Boston Elevated Railway for and during each of the years 1926 and 1927 is subject to an income tax imposed by the Revenue Act of 1926. The deficiency in tax

involved in each year arises wholly from the inclusion by the Commissioner of the petitioner's salary as trustee of the Boston Elevated Railway Company for the years in question.

Chapter 159 of the Special Acts of 1918 became duly operative by the performance of all conditions upon the happening of which the act was to take effect and was in operation during the years of 1926 and 1927. The petitioner, as a member of the board of trustees of said Boston Elevated Railway Company, created by and under said chapter 159, was engaged during said years 1926 and 1927 in exercising and performing the several powers and duties bestowed upon said board of trustees by said chapter 159.

Said act transferred to the board of trustees powers of management and operation previously vested in the board of directors of the private corporation. The powers thus transferred include the right to make contracts in the name of the corporation; to receive and pay out all income or other moneys to which it is
75 entitled; to issue stock, bonds, or promissory notes of the company; and to appoint and remove all officers of the company other than the board of directors.

Under said act the trustees are also given the right to regulate and fix fares, including the issue, granting, and withdrawal of transfers, and the imposition of charges therefor, and to determine the character and extent of the service and facilities to be furnished and "in these respects their authority shall be exclusive and shall not be subject to the approval, control, or direction of any other State board or commission." Powers were thus given the board of trustees which had been previously vested in and exercised by the public service commission of the Commonwealth of Massachusetts.

The Board of Tax Appeals, or any tribunal dealing with the petition in the above-entitled case, may take judicial notice of, and there are incorporated herein by reference, said chapter 159 of the Special Acts of Massachusetts for 1918 and the statements of fact so far as pertinent in the various decisions and opinions of the United States Supreme Court, of the Supreme Judicial Court of Massachusetts, and of the Board of Tax Appeals, wherein said act is discussed, and any other public laws of the United States or the Commonwealth of Massachusetts pertinent hereto; and also any additional matter contained in the taxpayer's petition and admitted by the respondent's answer filed herein.

STANLEY R. MILLER,
Petitioner.

C. M. CHAREST,
Attorney for Respondent.

Agreed to January 19, 1933.

C. M. CHAREST,
Attorney for Respondent.

Approved and ordered filed this twentieth day of January 1933.

CHARLES P. SMITH, *Member.*

76 Before United States Board of Tax Appeals

Docket No. 50575

STANLEY R. MILLER, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Statement of the evidence

Filed January 20, 1933

The above-entitled appeal was consolidated for hearing and decision with four other pending cases (Leland Powers, executor, no. 47836; Henry I. Harriman, no. 61846; Stanley R. Miller, no. 48007; Winthrop Coffin, no. 51029). The evidence consisted of stipulations of facts severally entered into by each petitioner and the respondent. The stipulation which constituted the entire evidence upon the above-entitled appeal was as follows:

It is hereby stipulated and agreed by and between the parties hereto as follows:

The petitioner is an individual residing at Brookline, Mass. The notice of deficiency (a copy of which is attached to the petition in this case, marked "Exhibit A") was mailed to the petitioner on September 26, 1930. This petition, Docket No. 50575, was filed with the Board of Tax Appeals November 1, 1930. The taxes in controversy are income taxes for the year 1928, said alleged deficiency being two hundred twenty-six dollars and ninety-two cents ($226.92) as set forth in said exhibit A.

On June 26, 1918, the petitioner was appointed by the Governor of the Commonwealth of Massachusetts, with the advise and consent of the executive council, a member of board of trustees of the Boston Elevated Railway Company, pursuant to the provisions of chapter 159 of the Special Acts of said Commonwealth for 1918, for a term of office expiring July 1, 1928, or thereafter on the qualification of a successor, and the petitioner, owning no stock or other securities of the Boston Elevated Railway Company or of any company owned, leased, or operated by it, thereupon qualified for said office by taking the oaths required by the constitution and the laws of
77 the Commonwealth of Massachusetts to be taken by public officials before entering upon the discharge of their duties. On December 26, 1928, the petitioner was reappointed by the Governor of the Commonwealth of Massachusetts, with the advise and consent of the executive council, a member of the board of trustees of said railway company, under the provisions of said chapter 159, for a further term of ten years from July 1, 1928, and he thereupon qualified for said office on December 27, 1928, by taking the oaths required by the constitution and the laws of the Commonwealth of Massachusetts to be taken by public officials before entering upon the discharge of their duties.

Throughout 1928 the petitioner, as a trustee of the Boston Elevated Railway Company, was an officer of the Commonwealth of Massachusetts, and by virtue of holding said office received as compensation therefor in said year the sum of five thousand dollars ($5,000) as provided in said chapter 159 of the Special Acts of 1918.

The Commissioner has held that this salary amounting to five thousand dollars ($5,000) received by the petitioner as a member of the board of trustees of the Boston Elevated Railway for and during 1928 is subject to an income tax imposed by the Revenue Act of 1926, and amendments thereto. The deficiency in tax involved arises wholly from the inclusion by the Commissioner of the petitioner's salary as trustee of the Boston Elevated Railway Company for the year in question.

[Memorandum. The remaining paragraphs of this statement of evidence being the same as those in no. 48007, except that the year 1928 is here substituted for the years 1926 and 1927, printed at pages 72 to 75, inclusive, are here omitted. A. I. Charron, clerk.]

STANLEY R. MILLER,
Petitioner.

C. M. CHAREST,
Attorney for Respondent.

Agreed to January 19, 1933.

C. M. CHAREST,
Attorney for Respondent.

Approved and ordered filed this twentieth day of January 1933.

CHARLES P. SMITH, *Member.*

78 Before United States Board of Tax Appeals

Docket No. 48007

[Title omitted.]

Docket No. 50575

Praecipe for record

Filed January 19, 1933

[Memorandum. This praecipe, being the same as that already printed at pages 50 and 51, is here omitted. A. I. Charron, clerk.]

STANLEY R. MILLER,
Petitioner, 31 Milk Street, Boston, Massachusetts.

JANUARY 7, 1933.

Service of a copy of the foregoing is hereby acknowledged this nineteenth day of January 1933.

C. M. CHAREST,
Attorney for Respondent.

[Clerk's certificate to foregoing transcript omitted in printing.]

79 [Memorandum. Orders of enlargement of time for docketing these petitions for review to and including April 15, 1933, are here omitted. A. I. Charron, clerk.]

81 In United States Circuit Court of Appeals, First Circuit

Minute entries

On August 1, 1933, motions for substitution of Guy T. Helvering, Commissioner of Internal Revenue, for David Burnet in each of five petitions for review, consolidated in this court by leave of court, were filed and allowed.

Thereafter, to wit, on October 5 and 6, 1933, this consolidated case came on to be heard by the court, Honorable Scott Wilson and Honorable James M. Morton, Jr., Circuit Judges, and Honorable Clarence Hale, District Judge, sitting.

83 In United States Circuit Court of Appeals for the First Circuit

No. 2811. October term, 1933

LELAND POWERS, EXECUTOR, ET AL., PETITIONERS FOR REVIEW

v.

COMMISSIONER OF INTERNAL REVENUE

Appeal from the Board of Tax Appeals

Before WILSON, MORTON, and HALE, JJ.

Opinion of the court

Filed January 9, 1934

MORTON, J.: The question is whether the public trustees of the Boston Elevated Railway Co. were subject to a Federal income tax on their official salaries for the years 1926–9. The Commissioner held that they were, and the Board of Tax Appeals affirmed his ruling. The facts are stated in the findings and opinion of the Board. (26 B.T.A. 1381.) There are differences between the cases of different petitioners as to the tax year, or years, which are involved; but these differences do not affect the legal questions before us.

The unusual arrangement under which the Commonwealth of Massachusetts took over the Boston Elevated Railway Co. has been the subject of much judicial consideration. (See Opinion of the Justices, 231 Mass. 603; Boston v. Treasurer, 237 Mass. 403; Opinion

of the Justices, 261 Mass. 523; Boston v. Jackson, 260 U.S. 309.)

It was, in substance, that the Railway Company turned over
84 its property to the Commonwealth for a term of years in return for guaranteed dividends on its stock and interest on its obligations; the railway continued to be operated under the company's charter, but by public officials, instead of by corporate officers. Under the statute (Acts of 1918, chap. 159), the Governor appointed, with the advice and consent of the executive council, five persons called "trustees" to act as managers of the railway. Their term of office was ten years; they were sworn to the faithful discharge of their duties; they were removable by the Governor and council; they were each paid $5,000 per year as salary; they had final power to fix rates, exercising as to this company powers otherwise vested in the public service commission; and they had authority, under certain circumstances, to declare deficits, which they apportioned among the communities served, and which were then included in the tax levy. The petitioners and their co-trustees were duly appointed and operated the railway during the years here in question, viz: 1926, 1927, 1928, and 1929.

The statutes involved are the Revenue Acts of 1926 and 1928 (44 Stat. 9; 45 Stat. 791); and the Treasury Regulations made under them. (Regulations 69, art. 88, act of 1926; Regulations 74, art. 643, act of 1928.) The controversy really arises out of the Treasury Regulations under the act of 1926, which was, in substance, repeated under the later act. It is as follows:

"ART. 88. Compensation of State officers and employees. Compensation paid to its officers and employees by a State or political subdivision thereof for services rendered in connection with the exercise of an essential governmental function of the State or political subdivision, including fees received by notaries public commissioned by States and the commissions of receivers appointed by State courts, is not taxable. Compensation received for services rendered to a State or political subdivision thereof is included in gross income unless (a) the person received such compensation as an officer or employee of a State or political subdivision, and (b) the services are rendered in connection with the exercise of an essential governmental function."

Two basic questions are presented, (1) Were the petitioners entitled to exemption under the regulation? (2) If not, is the
85 regulation, insofar as it denies them exemption, valid under established law? As to (1), the regulation exempts from the Federal income tax salaries of State officers or employees, if paid "for services rendered in connection with the exercise of an essential governmental function of the State." It is clear that the petitioners are public officers of the State. They hold offices created by a statute; they are appointed by the Governor with the advice and consent of the council; they may be removed by him with the consent of

the council; they are sworn to the faithful discharge of their duties; they exercise on behalf of the Commonwealth final power over rates of fare, being pro tanto a public service commission; they have power to declare and apportion deficits which are thereupon collected by taxation. The position which they hold has practically all the important characteristics of public office. Metcalf & Eddy v. Mitchell, Adm'x, 269 U.S. 514; Commissioner v. Ogden, 62 Fed. (2d) 334 (C.C.A. 1). While the statute says that for certain purposes they "shall not be considered public officers", it seems to us that for present purposes they are so. They have been so referred to by the Supreme Judicial Court (231 Mass. 603), and they have been held to be such by the Board of Tax Appeals in the case of Winthrop Coffin (12 B.T.A. 702), a decision which we do not understand has been overruled on that point by that in the case before us.

The Board of Tax Appeals, agreeing that the petitioners were "public officials as that term has been liberally interpreted", held that, "as they were not exercising governmental functions in the performance of their duties", they did not bring themselves within the exemption permitted by the regulation; that the regulation was valid according to its terms; and that the salaries were, therefore, taxable. It may be conceded that, judging by classical standards, the operation of a street railway is not an essential function of government (Flint v. Stone Tracy Co., 220 U.S. 107; So. Carolina v. United States, 199 U.S. 437),—although how long such standards of governmental function will be valid, in view of the present tendency to extend the field of governmental activities, is perhaps uncertain. But these trustees have much
86 greater power than merely to operate a street railway. They have the power, as has been pointed out, to fix rates, and to declare deficits which upon their decision were collected by taxation. Both these powers are by any standard essentially governmental. If a State officer exercises any powers of that character, his entire salary is, in our opinion, exempt by the regulation. We do not think it is the intention of the regulation that there should be an apportionment of exemption, that a certain part of the salary should be, more or less arbitrarily, allocated to the service of governmental character and exempted, while the rest of the salary is taxed —and no such contention is made. The salaries in question were therefore exempt under the regulations.

As to (2): On broader grounds also we are of the opinion that these salaries were not taxable. It has long been established that, in our curious, dual government, neither sovereign could tax the pay of officers of the other. Dobbins v. Commissioner 16 Peters 435; Buffington v. Day, 11 Wall. 113; Metcalf & Eddy v. Mitchell, Adm'x., 269 U.S. 514. In the case last cited, it was said, "It is on this principle that, as we have seen, any taxation by one government *of the salary of an officer of the other* . . . is prohibited." (Italics

supplied.) Stone, J., page 524. We are aware of no decision which holds that one sovereign may tax the salary of a *public officer* of the other, nor of any precedent for such discrimination in exemption as is set up by the regulation. No such ground of discrimination was suggested in the Metcalf & Eddy case, supra, although it was open on the facts, the plaintiff being a water-works engineer employed under contract by a public body. In Massachusetts, ownership and operation of water works by the public is not regarded as a governmental function. Lynch v. Springfield, 174 Mass. 430. In the Metcalf & Eddy case the government waived its appeal from the ruling of the District Court, that the salaries which the plaintiffs received as chief engineer of the Kennebec Water District, a political subdivision of Maine, and as a member of the North Shore Sanitary District, a political subdivision of Illinois, were exempt from Federal taxation, and in effect assented that such exemption was correct. The decisions relied upon by
87 the Government do not touch the question under discussion. They deal with the taxability of different kinds of commerce and industry—something quite different from the taxability of the salaries of State officers.

As a practical matter, the test adopted in the Treasury regulation opens a wide door for controversy, especially in view of the extension of government into new fields. Is it open to States to tax the salaries of all Federal officers except those employed on classical governmental functions? And vice versa? We do not think so.

That the salaries of the trustees were paid in the first instance by ahe railway company is not important. Fees of deputy sheriffs, of public administrators, of deputy marshals, of notaries public, and of many other officials of the Federal or State Governments, are not paid from the Public Treasury, but are nevertheless recognized as exempt from taxation by the other government. Moreover, during and at the close of the period under discussion, the railway company was heavily indebted to the Commonwealth for operating deficits which had been collected out of taxation. The salaries increased the deficits, and may well be regarded as having been paid by the public.

The decision of the Board of Tax Appeals is reversed and the case is remanded to that Board for further proceedings not inconsistent with this opinion.

In United States Circuit Court of Appeals

Final decree

January 9, 1934

This cause came on to be heard October 5 and 6, 1933, upon the record upon petition for review of the United States Board of Tax Appeals, and was argued by counsel.

Upon consideration whereof, it is now, to wit, January 9, 1934, here ordered, adjudged, and decreed as follows: The decision of the Board of Tax Appeals is reversed and the case is remanded
88 to that Board for further proceedings not inconsistent with the opinion passed down this day.

By the court.

ARTHUR I. CHARRON, *Clerk.*

Thereafter, to wit, on February 9, 1934, mandate issued to the United States Board of Tax Appeals.

[Clerk's certificate to foregoing transcript omitted in printing.]

89 Supreme Court of the United States

Order allowing certiorari

Filed May 14, 1934

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the First Circuit is granted. And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

(Endorsement on cover:) File no 38549. U. S. Circuit Court of Appeals, First Circuit. Term no. 17. Guy T. Helvering, Commissioner of Internal Revenue, petitioner, vs. Leland Powers, Executor, et al. Petition for a writ of certiorari and exhibit thereto. Filed April 9, 1934. File no. 17. O.T. 1934.

U. S. GOVERNMENT PRINTING OFFICE: 1934

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In the Supreme Court of the United States

OCTOBER TERM, 1933

No. —

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, petitioner

v.

LELAND POWERS, EXECUTOR, ET AL.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIRST CIRCUIT

The Solicitor General, on behalf of the Commissioner of Internal Revenue, prays that a writ of certiorari issue to review the judgment of the Circuit Court of Appeals for the First Circuit, entered in the above cause on January 9, 1934, reversing decisions of the Board of Tax Appeals.[1]

[1] The case involves the tax liability of five taxpayers. Five proceedings were begun before the Board; the cases were there consolidated and heard together. Five petitions for review were filed in the court below, but these were consolidated, and one judgment was entered. Accordingly, a single petition for certiorari is filed in this Court.

OPINIONS BELOW

The opinion of the Circuit Court of Appeals (R. 81–84) is reported in 68 F. (2d) 634. The findings of fact and opinion of the Board of Tax Appeals (R. 24–40) are reported in 26 B.T.A. 1381.

JURISDICTION

The judgment of the court below was entered January 9, 1934. (R. 84.) The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the income received by the taxpayers as trustees of the Boston Elevated Railway Company was exempt from Federal taxation on the ground that such a tax would be an unconstitutional burden on the State.

STATUTES AND REGULATIONS INVOLVED

The Federal statutes and regulations involved are set forth in Appendix A (*infra,* pp. 15–16). The material portions of the Special Act of the Massachusetts Legislature providing for the public operation of the Boston Elevated Railway Company are set forth in Appendix B (*infra,* pp. 17–26).

STATEMENT

The facts as found by the Board of Tax Appeals (R. 24–29) may be summarized as follows:

Prior to 1926 the taxpayers were appointed trustees of the Boston Elevated Railway Company

under the provisions of Chapter 159 of the Special Acts of 1918 of the Commonwealth of Massachusetts, "An Act to Provide for the Public Operation of the Boston Elevated Railway Company." The material portions of this Act are set out in Appendix B, *infra,* p. 17.

Under this Special Act the State, with the consent of the company, took over the management and operation of the railway and the properties of the company in return for guaranteed dividends on its stock and interest on its obligations. The property remained at all times that of the company, the State taking over only the management and operation, which was to continue for a period of ten years or such extended period as might be determined. There was created a board of trustees, consisting of five persons to be appointed by the Governor with the advice and consent of the Executive Council, to manage and operate the railway and to hold possession of the properties of the company on behalf of the State during the period of public operation. The trustees were appointed for a term of ten years and it was provided (Sec. 1) that each should receive "from the company" an annual salary of $5,000. The trustees were vested with all the rights and powers of the company and its directors, were authorized to receive and disburse its income and funds, and determine the service and facilities to be furnished, in which latter respects their authority was exclusive of control

by any other state Board or Commission. It was provided that the trustees should not be considered public officers for certain purposes, and (Sec. 2) in the management and operation of the company and its properties they should "be deemed to be acting as agents of the company and not of the commonwealth."

The trustees were authorized to fix such rates of fare as reasonably necessary to produce sufficient income to meet the cost of service including therein, among other items referred to, dividends on the stock. Out of the bond issue authorized to be made by the company the trustees were to set up a reserve fund to pay the cost of service when revenues were inadequate, with provision that semiannually any deficiency in the reserve fund for that purpose would be supplied by the State and at like periods any excess of the reserve fund over the original amount should be applied to reimburse the State for amounts paid to the company. Such amounts as the State might be required to pay the company were to be obtained by assessment, in addition to state taxes, proportionately upon the cities and towns served by the company and any excess revenues repaid to the State were to be distributed proportionately to such cities and towns. Upon termination of public management and operation the company was authorized to take over the management and operation. Upon resumption of private operation the company was to

fix and collect such reasonable fares as would produce sufficient income to pay the cost of service, to the same extent as the trustees were so authorized, with authority also to establish schedules of fares automatically increasing or decreasing in the same manner as authorized in the case of the trustees. After the return of control to the company, however, the State no longer was obligated to supply any deficiency in income. It was provided that public regulation and supervision of the company after resumption of private operation should not be exercised so as to reduce the income below the reasonable cost of service as defined, which included dividends on stock and interest on obligations.

In 1919 a deficiency of $3,980,151.67 was incurred from public operation of the railway, which amount the State obtained by apportionment among the cities and towns served and paid it to the company in accordance with its obligation under the Act. The excess revenues from operations up to and including 1929 were insufficient to fully reimburse the State and cities and towns for the sum so paid.

During the respective taxable years each taxpayer was a trustee of the Boston Elevated Railway and received a salary of $5,000 per year, under the Special Act. The Commissioner determined that the salary so received by each taxpayer was

taxable income and asserted a deficiency against each taxpayer for the respective years.

The Board of Tax Appeals sustained the Commissioner (R. 40), but this decision was reversed by the Circuit Court of Appeals (R. 84).

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred:

1. In holding that the taxpayers as trustees of the Boston Elevated Railway Company, having been appointed under a Special Act of the Massachusetts legislature providing for public management and operation of the railway properties, were exercising essential governmental functions of the State and hence their salaries were exempt from Federal taxation.

2. In holding that the compensation received by the taxpayers as such trustees was not subject to the Federal income tax.

3. In holding invalid the provisions of Article 88 of Treasury Regulations 69.

4. In reversing the decisions of the Board of Tax Appeals.

REASONS FOR GRANTING THE WRIT

1. The decision below extends the doctrine of implied exemption beyond its proper scope and in so doing is apparently in conflict with the decisions of this Court in *Flint* v. *Stone Tracy Co.*, 220 U.S. 107, and *South Carolina* v. *United States*, 199 U.S. 437. In the *Stone Tracy* case, this Court said (p. 172):

> It is no part of the essential governmental functions of a State to provide means of transportation, supply artificial light, water, and the like. * * *
>
> The true distinction is between the attempted taxation of those operations of the States essential to the execution of its governmental functions, and which the State can only do itself, and those activities which are of a private character.

The decision also appears to be in conflict in this respect with the decision of the Circuit Court of Appeals for the Eighth Circuit in *State of North Dakota* v. *Olson*, 33 F. (2d) 848, appeal dismissed, 280 U.S. 528. In that case the court pointed out (p. 852) that there is a distinction between "public purpose" and "governmental purpose", a distinction which the court below appears to have ignored.

2. The decision below holds invalid an important regulation promulgated by the Treasury Department for the administration of the tax laws. In Article 88 of Regulations 69, it is provided:

> ART. 88. *Compensation of State officers and employees.*—Compensation paid to its officers and employees by a State or political subdivision thereof for services rendered in connection with the exercise of an essential governmental function of the State or political subdivision, including fees received by notaries public commissioned by States and the commissions of receivers appointed by State courts, is not taxable. Compensation received for services rendered to a State or

> political subdivision thereof is included in gross income unless (a) the person receives such compensation as an officer or employee of a State or political subdivision, and (b) the services are rendered in connection with the exercise of an essential governmental function. * * *

Article 643 of Regulations 74 and Article 643 of Regulations 77, promulgated under succeeding Revenue Acts, are the same. The regulation, therefore, has received the approval of Congress through reenactment of the statute upon which it is based. *United States* v. *Dakota-Montana Oil Co.*, 288 U.S. 459, 466.

The court below held this regulation invalid, saying (R. 83) that it was aware of no "precedent for such discrimination in exemption as is set up by the regulation." The "discrimination" referred to was, of course, the distinction made between services rendered in connection with the exercise of an essential governmental function and services not rendered in connection with such a function. This distinction finds its basis in the explicit decisions of this Court in *South Carolina* v. *United States, supra,* and *Flint* v. *Stone Tracy Co, supra.* In denying the validity of this distinction, the decision below is in conflict with these two decisions of this Court, and also with the decision in *Blair* v. *Byers,* 35 F. (2d) 326 (C.C.A. 8th).

3. The decision below is erroneous. The statute of Massachusetts under which the taxpayers

were appointed specifically provided that each should "receive *from the company* as compensation for his services five thousand dollars annually." (Italics ours.) The compensation in question, therefore, was not paid by the Commonwealth of Massachusetts, but by the company. In holding that the payments were nevertheless exempt from Federal taxation, the decision below is inconsistent with *Miller* v. *McCaughn*, 27 F. (2d) 128 (C.C.A. 3d).[2]

In Section 2 of the statute (*infra*, p. 18) it was provided that in the management and operation of the property, the trustees should "be deemed to be acting as agents of the company and not of the commonwealth." It was also provided in the same section that—

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[2] The court below seeks to avoid this question by saying that during the period in question the Railway Company was indebted to the Commonwealth, that the deficits had been collected out of taxation, "and may well be regarded as having been paid by the public" (R. 84). But the advances by the Commonwealth were, as the court says, debts of the company. The salaries, therefore, were no more paid by the Commonwealth than the salaries of officers of a business corporation are paid by its bondholders or other creditors. The primary obligation was on the company. Though the Commonwealth made up the deficit, it expected reimbursement. Moreover, there is nothing whatever in the record to show that the company operated at a deficit during the years in question, or in any year other than 1919. (See R. 29.) There is consequently no basis for saying that the particular salaries here involved were not paid by the company and by the company alone.

> Nothing herein contained shall be held to affect the right of the commonwealth or any subdivision thereof to tax the company or its stockholders in the same manner and to the same extent as if the company had continued to manage and operate its own property.

These provisions of the statute show plainly enough the nature of the positions held by the trustees. They were "agents of the company and not of the commonwealth." The provision that the Commonwealth and its subdivisions should retain the right to tax the property shows that the Commonwealth itself did not regard the operation of the railroad as one of its normal functions. As the court said in *Boston Elevated R. Co.* v. *Malley,* 24 F. (2d) 758, 759 (D.Mass.), concerning the same provision of the statute—

> It would be a curious arrangement under which the corporation continued to be fully taxable as such for the benefit of the commonwealth, while it escaped taxation by the federal government.

In this decision and in *Boston Elevated R. Co.* v. *Malley,* 288 Fed. 864 (D.Mass.), it was held that the Boston Elevated Railway Company itself was subject to Federal taxation. The decision below is therefore contrary to these decisions.* The deci-

* The effect of the decision below is, of course, to overrule these two decisions, since they are by District Courts in the same Circuit.

sion is also contrary in this respect to the decisions of the Board of Tax Appeals in *Wanless Iron Co.* v. *Commissioner,* 29 B.T.A. 834, and *Hobart Iron Co.* v. *Commissioner,* 29 B.T.A. 855. In these cases it was held that the income of a lessee of State ore lands was subject to Federal taxation where the lease contained a provision that the lands should be subject to taxation as if they were owned in fee by the lessee. Cf. *Bass* v. *Group No. 1 Oil Corp.,* 41 F. (2d) 483 (C.C.A. 5th), affirmed on other grounds, 283 U.S. 279.

The court below seems to have based its decision largely on the ground of the authority conferred on the trustees to fix rates and to declare deficits which were to be collected through taxation. (See R. 83.) But the basis upon which the rates were to be fixed was provided for in detail in the Act itself. See Sections 6–11 (*infra,* pp. 20–23). Cf. *Cleveland Railway Co.* v. *Commissioner,* 36 F. (2d) 347 (C.C.A. 6th), certiorari denied, 281 U.S. 743. The trustees were given substantially no discretion, and were not required to make determinations on questions involving the exercise of judgment, such as the valuation of the property. The authority conferred on the trustees in this respect was essentially the same as the authority conferred on the company itself when private operation should be resumed. See Section 15 (*infra,* pp. 25–26). The trustees had no power to levy taxes. They could only certify the amount of any deficit to the Treas-

urer and Receiver General of the Commonwealth, and the State imposed the necessary tax. The primary duty of the trustees was to operate the railroad and at rates of fare which would meet all charges. The operation was for private profit, for under the Special Act the trustees were to declare dividends "upon the preferred and common stock of the company, and provide for the payment of the same." Sec. 3 (*infra,* p. 20); see also Sec. 6 (*infra,* pp. 20–21).

4. The decision below, if allowed to stand, will greatly increase the field of exemption of state instrumentalities from Federal taxation. It is obvious, therefore, that the decision presents a question of considerable public importance, representing, as it does, another instance of the growing tendency of some of the lower Federal courts to extend the doctrine of implied immunity to such a degree that, if unchecked, the Federal revenue will be materially affected.[4] Some of the States, since the repeal of the Eighteenth Amendment to the Constitution, have undertaken the sale of liquor through state dispensaries, and the State of Ohio has already sought leave from this Court to file a bill in equity seeking to enjoin Federal officers from taxing this enterprise carried on by the State. *State of Ohio* v. *Helvering,* No. —, Original.

[4] A similar question was involved in *Commissioner* v. *Sherman*, C.C.A. 1st, decided March 14, 1934, in which the court below also held the income exempt from Federal taxation.

Other States have created boards or commissions for the operation of ports or terminal facilities. The power of the Federal Government to tax these activities and the agencies employed in conducting them is already being questioned. The court below recognized "the present tendency to extend the field of governmental activities" in its opinion (R. 83), and seemed to regard this tendency as a reason for extending the sphere of tax exemption. Yet, it was this extension of governmental activity with its accompanying threat to the Federal revenues which was the very basis of this Court's decision in *South Carolina* v. *United States,* 199 U.S. 437, 454–455, 457.

This Court has recently granted writs of certiorari on the Government's petition in two similar cases, both of which were reversed *per curiam*. *Lucas* v. *Howard,* certiorari granted, 279 U.S. 830, reversed, 280 U.S. 526; *Lucas* v. *Reed,* certiorari granted, 280 U.S. 549, reversed, 281 U.S. 699. The decisions of this Court in those cases have served largely to put to rest questions of the taxability of income received by a taxpayer from a State for services as special counsel or the like. See, e.g., *Burnet* v. *McDonough,* 46 F. (2d) 944 (C.C.A. 8th); *Lewis* v. *Commissioner,* 47 F. (2d) 32 (C.C.A. 3d); *Haight* v. *Commissioner,* 52 F. (2d) 779 (C.C.A. 7th); *Register* v. *Commissioner,* C.C.A. 5th, decided March 10, 1934. A decision by this Court in the present case is required to remove the

uncertainty and confusion which is bound to follow from the decision of the court below striking down the distinction for tax purposes, so far as officers are concerned, between essential governmental functions and other activities carried on by a State.

Wherefore, it is respectfully submitted that this petition for a writ of certiorari should be granted.

J. CRAWFORD BIGGS,
Solicitor General.

APRIL 1934.

APPENDIX A

Revenue Act of 1926, c. 27, 44 Stat. 9:

SEC. 212. (a) In the case of an individual the term "net income" means the gross income as defined in section 213, less the deductions allowed by sections 214 and 206.

* * * * *

(U.S.C.App., Title 26, Sec. 953.)

SEC. 213. For the purposes of this title, except as otherwise provided in section 233—

(a) The term "gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service * * * of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property * * * or gains or profits and income derived from any source whatever. The amount of all such items shall be included in the gross income for the taxable year in which received by the taxpayer, unless, under methods of accounting permitted under subdivision (b) of section 212, any such amounts are to be properly accounted for as of a different period.

* * * * *

(U.S.C.App., Title 26, Sec. 954.)

Revenue Act of 1928, c. 852, 45 Stat. 791, 797:

Sections 21 and 22 (a) of the Revenue Act of 1928, so far as material, are substantially the same as Sections 212 (a) and 213 (a), respectively, of the Revenue Act of 1926, set forth above.

Treasury Regulations 69, promulgated under the Revenue Act of 1926:

> ART. 88. *Compensation of State officers and employees.*—Compensation paid to its officers and employees by a State or political subdivision thereof for services rendered in connection with the exercise of an essential governmental function of the State or political subdivision, including fees received by notaries public commissioned by States and the commissions of receivers appointed by State courts, is not taxable. Compensation received for services rendered to a State or political subdivision thereof is included in gross income unless (*a*) the person receives such compensation as an officer or employee of a State or political subdivision, and (*b*) the services are rendered in connection with the exercise of an essential governmental function. But see section 1211 as to 1924 and prior years.

Treasury Regulations 74, promulgated under the Revenue Act of 1928:

Article 643 of Regulations 74, so far as material, is substantially the same as Article 88 of Regulations 69, set forth above.

APPENDIX B

Massachusetts, Special Acts and Resolves, 1918:

Chap. 159. AN ACT TO PROVIDE FOR THE PUBLIC OPERATION OF THE BOSTON ELEVATED RAILWAY COMPANY

Be it enacted, etc., as follows:

SECTION 1. The board of trustees of the Boston Elevated Railway Company is hereby created, to consist of five persons to be appointed by the governor, with the advice and consent of the council. The persons so appointed shall be sworn before entering upon the performance of their duties; shall own no stock or other securities of the Boston Elevated Railway Company or of any company owned, leased, or operated by it; shall serve for the term of ten years from the date when they assume the management of the company as hereinafter provided and until their successors are duly appointed and qualified, and each shall receive from the company as compensation for his services five thousand dollars annually. In case of any vacancy in said board by reason of death, resignation or otherwise, the governor, by and with the consent of the council, shall fill the vacancy. The board shall designate one of the trustees so appointed to serve as chairman. Any member of the board may be removed for cause by the governor, with the advice and consent of the council.

Said trustees shall not be considered public officers within the meaning of section twenty-five of chapter five hundred and fourteen of the acts of nineteen hundred and nine, but shall be subject in all other respects to the provisions of said section to the same extent as are the directors of the Boston Elevated Railway Company, but said section shall not apply to recommendations by the governor to said trustees. The provisions of section one of chapter seven of the Revised Laws shall not apply to the said board.

If the public management and operation of the railway system of the Boston Elevated Railway Company shall continue beyond the original period of ten years the governor shall, with the advice and consent of the council, at the expiration of each ten-year period during the continuance of public management and operation, appoint five successor trustees to serve for a period of ten years and until their successors are appointed and qualified, but not exceeding the period of public management and operation. Said trustees shall assume the management and operation of the company's property on the first day of the month next following their appointment and qualification.

SECTION 2. Said board of trustees, hereinafter called the trustees, shall manage and operate the Boston Elevated Railway Company hereinafter called the company, and the properties owned, leased or operated by it, for a period of ten years, commencing on the first day of the month next after their appointment and qualification, and, subject to the provisions of this act, shall take and have possession of said properties in behalf of the commonwealth during the period of

public operation, and, for the purposes of this act, shall, except as is otherwise provided in this act have and may exercise all the rights and powers of said company and its directors, and, upon behalf of said company, shall receive and disburse its income and funds. They shall have the right to appoint and remove in their discretion the president, treasurer and clerk of the corporation, and all officers of the company other than the board of directors. They shall have the right to regulate and fix fares, including the issue, granting and withdrawal of transfers, and the imposition of charges therefor, and shall determine the character and extent of the service and facilities to be furnished, and in these respects their authority shall be exclusive and shall not be subject to the approval, control or direction of any other state board or commission.

In the management and operation of the said company and of the properties owned, leased or operated by it, as authorized by this act, the trustees and their agents, servants and employees shall be deemed to be acting as agents of the company and not of the commonwealth, and the company shall be liable for their acts and negligence in such management and operation to the same extent as if they were in the immediate employ of the company, but said trustees shall not be personally liable. A majority of the board shall constitute a quorum for the transaction of business, and the action of a majority of those present at any meeting shall be deemed the action of the trustees.

Nothing herein contained shall be held to affect the right of the commonwealth or any subdivision thereof to tax the company or its

stockholders in the same manner and to the same extent as if the company had continued to manage and operate its own property.

SECTION 3. The trustees shall have authority to make contracts in the name and on behalf of, and to issue stocks, bonds and other evidences of indebtedness of, the company. * * *

The trustees shall cause to be paid all amounts which may from time to time become due from the company, and shall declare dividends at the appointed times upon the preferred and common stock of the company, and provide for the payment of the same.

SECTION 5. The Boston Elevated Railway Company shall, prior to or at the time of its acceptance of this act, provide for raising three million dollars in cash by the issue of preferred stock at not less than the par value which shall be one hundred dollars per share. * * *

One million dollars shall be set aside as a reserve fund to be used only for the purposes hereinafter specified, and the remaining two million dollars shall be subject to the disposition of the trustees to pay for the cost of additions and improvements to the company's property.

SECTION 6. The trustees shall from time to time, in the manner hereinafter provided, fix such rates of fare as will reasonably insure sufficient income to meet the cost of the service, which shall include operating expenses, taxes, rentals, interest on all indebtedness, such allowance as they may deem necessary or advisable, for depreciation of property and for obsolescence and losses in respect to property sold, destroyed, or abandoned, all other expenditures and charges which under the laws of the commonwealth

now or hereafter in effect may be properly chargeable against income or surplus, fixed dividends on all preferred stock of the company from time to time outstanding, and dividends on the common stock of the company from time to time outstanding at the rate of five percent per annum on the par value thereof during the first two years, five and one half percent per annum on the par value thereof during the next two years and six percent per annum on the par value thereof during the balance of the period of public operation. * * *

SECTION 7. The trustees shall, within sixty days after their appointment and qualification, fix and put in operation rates of fare which in their judgment will produce sufficient income to meet the cost of the service as defined in section six, and within sixty days thereafter shall adopt and publish a schedule of eight different grades of fare, of which four shall be below and four above the rate of fare first established; and whenever by reason of any change in the existing rate of fare there are less than four grades, either above or below the rate then in force, the trustees shall forthwith adopt and publish a schedule of additional grades of fare so that there shall always be not less than four grades of fare above and below the existing rate of fare.

If at any time the trustees shall be of opinion that said rates of fare or schedule should be changed, either with regard to the method or basis upon which the fares and transfer privileges are established, or because the steps between the different grades are too small or too great, or for any other reason, the trustees may adopt, publish, and put in effect new schedules or rates of fare

to take the place of the existing schedule or rates of fare.

SECTION 8. The reserve fund shall be used only for the purpose of making good any deficiency in income as provided in section nine or for reimbursing the commonwealth as provided in sections eleven and thirteen, and until such use, may be invested in income-producing securities in the discretion of the trustees, and all income or interest received thereon shall be treated as part of the general income of the company.

SECTION 9. Whenever the income of the company is insufficient to meet the cost of the service as herein defined, the reserve fund shall be used as far as necessary to make up such deficiency, and whenever, on the other hand, such income is more than sufficient to meet the cost of the service, the excess shall be transferred to and become a part of the reserve fund.

SECTION 10. If, as of the last day of June in the year nineteen hundred and nineteen, or the last day of any September, December, March or June thereafter, the amount of the reserve fund shall exceed by thirty percent or more the amount originally established, and during the preceding three months the income shall have exceeded the cost of the service, the trustees shall within one month thereafter put into effect the next lower grade of fare that has been adopted as provided in section seven; and if, as of any such last day of June, September, December or March, the amount of the reserve fund shall be less than seventy percent of the amount originally established and during the preceding three months the income has been less than the cost of the service, the trustees shall within one month there-

after put into effect the next higher grade of fare, and the fare shall continue to be decreased or increased, as the case may be, subject to the same conditions, if the amount of the reserve fund is above or below said limits, as of such quarterly dates. In determining the amount of the reserve fund for the purposes of this section only there shall first be deducted therefrom any amounts which have been paid by the commonwealth to the company under the provisions of section eleven, and for which the commonwealth has not been reimbursed.

SECTION 11. If, as of the last day of June in the year nineteen hundred and nineteen, or the last day of any December or June thereafter, the amount remaining in the reserve fund shall be insufficient to meet the deficiency mentioned in section nine, it shall be the duty of the trustees to notify the treasurer and receiver general of the commonwealth of the amount of such deficiency, less the amount, if any, in the reserve fund applicable thereto, and the commonwealth shall thereupon pay over to the company the amount so ascertained. Pending such payment it shall be the duty of the trustees to borrow such amount of money as may be necessary to enable them to make all payments, including dividend payments, as they become due. If, as of the last day of any June or December thereafter during the period of public operation, the reserve fund shall exceed the amount originally established, the trustees shall apply the excess, so far as necessary, to reimbursing the commonwealth for any amounts which it may have paid to the company under the provisions hereof, and the commonwealth shall thereupon distribute the amount so received among the

cities and towns in which the company operates, in proportion to the amounts which they have respectively been assessed as provided in section fourteen.

In order to meet any payment required of the commonwealth under the provisions of this section the treasurer and receiver general may borrow at any time, in anticipation of the assessments to be levied upon the cities and towns, such sums of money as may be necessary to make said payments, and he shall repay any sums so borrowed as soon after said assessments are paid as is expedient.

SECTION 13. It shall be the duty of the trustees to maintain the property of the company in good operating condition and to make such provision for depreciation, obsolescence and rehabilitation, that, upon the expiration of the period of public management and operation, the property shall be in good operating condition. If the period of public management and operation expires, control of the property shall then revert to the company, and if at that time the reserve fund shall be less than the amount originally established because the income during the period of public management and operation has been insufficient to pay the cost of the service, the commonwealth shall forthwith pay over to the company an amount sufficient to restore it to its original amount; and if the amount in said reserve fund is then in excess of the amount originally established and any amount required to meet the cost of the service to the expiration of such period, such excess shall be paid into the treasury of the commonwealth and distributed among the cities and towns in which the company operates in the same

proportions as the assessments provided for by section fourteen.

SECTION 14. In case the commonwealth shall be called upon to pay to the trustees or the company any amount under the provisions of sections eleven and thirteen, such amount with interest or other charges incurred in borrowing money for the purpose shall be assessed upon the cities and towns in which the company operates by an addition to the state tax next thereafter assessed in proportion to the number of persons in said cities and towns using the service of the company at the time of said payment, said proportion to be determined and reported to the treasurer and receiver general by the trustees from computations made in their discretion for the purpose.

SECTION 15. Upon the termination of the period of public management and operation, the company shall manage and operate the property and may fix and collect such just and reasonable fares as will produce an income sufficient to pay the reasonable cost of the service as defined in section six, including dividends upon the common stock from time to time outstanding of six percent per annum on the par value thereof but no more, and may establish schedules of fares which shall automatically increase or decrease in the same manner as is authorized in the case of the trustees: *provided,* that the commonwealth shall be under no liability to make any payments to the company by reason of any deficiencies in income accruing after the discontinuance of public operation. The company shall thereafter be subject to public regulation and supervision in such manner as may be determined by the general court, but such regulation and supervision

shall not be exercised so as to reduce the income below the reasonable cost of the service as defined in this act.

SECTION 18. With the exception of section five, which shall take effect upon the passage of this act, this act shall take effect upon its acceptance by the holders of not less than a majority of all the stock of the Boston Elevated Railway Company and by the holders of not less than a majority of all the stock of the West End Street Railway Company, given at meetings called for the purpose, and the filing of certificates of acceptances with the secretary of the commonwealth, and the filing with the said secretary of a certificate, signed and sworn to by a majority of the directors of the Boston Elevated Railway Company, that the entire three million dollars of preferred stock provided for by section five has been subscribed for, and at least thirty percent of his subscription has been paid in in cash by each subscriber, and that no dividends have been declared or paid upon the company's common stock since the passage of this act.

* * * * *

U. S. GOVERNMENT PRINTING OFFICE: 1934

In the Supreme Court of the United States

OCTOBER TERM, 1933

No. 946

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, petitioner

v.

LELAND POWERS, EXECUTOR, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI, TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIRST CIRCUIT

REPLY BRIEF FOR THE PETITIONER

The respondents contend that the decision of the court below presents no question which this Court will care to review. In support of this contention the respondents argue that the decision below is predicated upon the ground that under the Special Act of the Massachusetts legislature they, as trustees of the Boston Elevated Railway, were not only public officers of the State, but also were exercising essential governmental functions and hence, under the terms of the regulations of the Treasury Department, compensation received by the respond-

ents was exempt from Federal income taxation. The respondents attempt to characterize the broader grounds which the court below invoked in support of its conclusion as dictum. Upon this premise the respondents assert that the decision below does not necessarily hold invalid the regulations of the Treasury Department and does not necessarily present an important question of constitutional law.

The decision below is predicated upon two grounds; first, that under the Massachusetts Special Act the trustees were public officers exercising essential governmental functions in that they were authorized to fix rates and declare deficits which upon certification to the state treasurer were to be raised by taxation. In this view the court below concluded that the compensation of the respondents as trustees was exempt from income taxation under the terms of the Treasury Department regulations. Second, that irrespective of the character of the functions performed by the trustees their compensation was exempt from the income tax merely by virtue of their status as public officers of Massachusetts. The opinion of the court below makes it plain that the decision is rested upon two grounds, either of which the court deemed sufficient to support the judgment. It cannot fairly be said that the decision is rested upon either ground to the exclusion of the other. There is no room in the opinion for the characterization of the

broader grounds upon which the decision is rested as dictum.

With respect to the first ground of the decision, we have pointed out that the authority conferred on the trustees to fix rates and to declare deficits was essentially the same as the authority conferred on the company itself when private operation should be resumed. There is nothing in the nature of such authority which partakes of a governmental character. The exercise of such authority by the trustees is no more governmental than the exercise of the same or like authority by the private corporation which owned the property. It is only by virtue of this erroneous conception of the duties and powers exercised by the trustees that the court below could reach the conclusion that the compensation of the trustees was exempt from the Federal income tax under the provisions of the Treasury Department regulations. If, as we contend, the powers conferred upon and exercised by the trustees were simply the management and operation of the street railway and were in nowise governmental, it is plain that under the Treasury regulations their compensation would not be exempt. The first ground of the court's decision therefore presents directly the question whether the trustees appointed under the Special Act solely for the management and operation of the street railway were engaged in exercising essential governmental functions of the State. The conclusion of the court be-

low upon this question is, as we have pointed out in the petition, inconsistent if not directly in conflict with decisions of this Court and decisons of other Circuit Courts of Appeals. That question, we submit, is one of public importance and merits a review and decision of this Court.

The second ground of the decision upon which the court placed as great if not greater reliance was that the trustees, as public officers of the State, were exempt from Federal income taxation for that reason alone. The court in that connection held expressly that the Treasury regulations, under which compensation of state officers and employees is exempt from Federal income taxation only if such officers or employees are engaged in exercising essential governmental functions, are invalid. As we pointed out in the petition, the holding of the court below that state agencies or instrumentalities, whether or not engaged in the exercise of governmental functions are exempt from Federal taxation, is in conflict with decisions of this Court and of other Circuit Courts of Appeals. In holding that a state officer is exempt from Federal income taxation merely by virtue of his official position, whether or not he be engaged in the exercise of governmental functions, the court below extends the doctrine of implied immunity of the agencies of one government from taxation by the other beyond its proper scope and ignores the underlying reasons for and the necessary limitations upon the doctrine as re-

peatedly declared by this Court. Cf. *Willcuts* v. *Bunn*, 282 U.S. 216, 225; *Board of Trustees* v. *United States*, 289 U.S. 48, 59.

The decision of the court below, upon either or both of the grounds stated in its opinion, presents a question of distinct public importance. Upon either ground the decision below is inconsistent, if not in direct conflict, with decisions of this Court and of other Circuit Courts of Appeals. The respondents state that the decision depends on its own peculiar facts. It is of course true of all cases of this sort that the facts on which they arise vary, but the decision below does not depend on these facts. It is of broad and sweeping application, and if erroneous, and if allowed to stand, it will certainly tend to the development of an unwarranted extension of the field of implied immunity. Such a decision, we submit, falls within the class of cases which should be reviewed by this Court.

We respectfully submit that the petition should be granted.

J. CRAWFORD BIGGS,
Solicitor General.
JOHN MACC. HUDSON,
ERWIN N. GRISWOLD,
Special Assistants to the Attorney General.

MAY 1934.

U. S. GOVERNMENT PRINTING OFFICE: 1934

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In the Supreme Court of the United States

OCTOBER TERM, 1934

No. 17

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, petitioner

v.

LELAND POWERS, EXECUTOR, ET AL.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIRST CIRCUIT

BRIEF FOR THE PETITIONER

OPINIONS BELOW

The opinion of the Circuit Court of Appeals (R. 57–60) is reported in 68 F. (2d) 634. The findings of fact and opinion of the Board of Tax Appeals (R. 17–29) are reported in 26 B.T.A. 1381.

JURISDICTION

The judgment of the court below was entered January 9, 1934 (R. 60–61). The petition for writ of certiorari was filed April 9, 1934, and was granted May 14, 1934 (R. 61). The jurisdiction of this Court rests on Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the income received by the taxpayers as trustees of the Boston Elevated Railway Company was exempt from Federal taxation on the ground that such a tax would be an unconstitutional burden on the State.

STATUTES AND REGULATIONS INVOLVED

The Federal statutes and regulations involved are set forth in Appendix A (*infra,* pp. 34–35). The material portions of the Special Act of the Massachusetts Legislature providing for the public operation of the Boston Elevated Railway Company are set forth in Appendix B (*infra,* pp. 36–45).

STATEMENT

The facts as found by the Board of Tax Appeals (R. 18–21) may be summarized as follows:

Prior to 1926 the taxpayers were appointed trustees of the Boston Elevated Railway Company under the provisions of Chapter 159 of the Special Acts of 1918 of the Commonwealth of Massachusetts, "An Act to Provide for the Public Operation of the Boston Elevated Railway Company." The material portions of this Act are set out in Appendix B, *infra.*

Under this Special Act the State, with the consent of the company, took over the management and operation of the railway and the properties of the company in return for guaranteed dividends on its stock and interest on its obligations. The

property remained at all times that of the company, the State taking over only the management and operation, which was to continue for a period of ten years or such extended period as might be determined. There was created a board of trustees, consisting of five persons to be appointed by the Governor with the advice and consent of the Executive Council, to manage and operate the railway and to hold possession of the properties of the company on behalf of the State during the period of public operation. The trustees were appointed for a term of ten years and it was provided (Sec. 1) that each should receive "from the company" an annual salary of $5,000. The trustees were vested with all the rights and powers of the company and its directors; were authorized upon behalf of the company to receive and disburse its income and funds and to determine the service and facilities to be furnished, in which latter respects their authority was exclusive of control by any other state board or commission. It was provided that the trustees should not be considered public officers for certain purposes (Sec. 1), and in the management and operation of the company and its properties they should "be deemed to be acting as agents of the company and not of the commonwealth, and the company shall be liable for their acts and negligence in such management and operation to the same extent as if they were in the immediate employ of the company" (Sec. 2).

The trustees were authorized to fix such rates of fare as reasonably necessary to produce sufficient income to meet the cost of service including therein, among other items referred to, dividends on the stock. Out of the three million dollars to be raised in cash by the company from the sale of preferred stock, the trustees were to set up a reserve fund of a million dollars to pay the cost of service when revenues were inadequate, with provisions that, semiannually, any deficiency in the reserve fund for that purpose would be supplied by the State and at like periods any excess of the reserve fund over the original amount should be applied to reimburse the State for amounts paid to the company. The remaining two million dollars were subject to the disposition of the trustees to pay for the cost of additions and improvements to the company's property (sec. 5). Such amounts as the State might be required to pay the company were to be obtained by assessment, in addition to state taxes, proportionately upon the cities and towns served by the company and any excess revenues repaid to the State were to be distributed proportionately to such cities and towns. Upon termination of public management and operation the company was authorized to take over the management and operation. Upon resumption of private operation the company was to fix and collect such reasonable fares as would produce sufficient income to pay the cost of service, to the same extent as the trustees were so authorized, with

authority also to establish schedules of fares automatically increasing or decreasing in the same manner as authorized in the case of the trustees. After the return of control to the company, however, the State no longer was obligated to supply any deficiency in income. It was provided that public regulation and supervision of the company after resumption of private operation should not be exercised so as to reduce the income below the reasonable cost of service as defined, which included dividends on stock and interest on obligations.

In 1919 a deficiency of $3,980,151.67 was incurred from public operation of the railway, which amount the State obtained by apportionment among the cities and towns served and paid it to the company in accordance with its obligation under the Act. The excess revenues from operations up to and including 1929 were insufficient to fully reimburse the State and cities and towns for the sum so paid.

During the respective taxable years, each taxpayer was a trustee of the Boston Elevated Railway and received a salary of $5,000 per year, under the Special Act. The Commissioner determined that the salary so received by each taxpayer was taxable income and asserted a deficiency against each taxpayer for the respective years. The taxable years involved are 1926 to 1929, inclusive (R. 17).

The Board of Tax Appeals sustained the Commissioner (R. 29), but its decision was reversed by the Circuit Court of Appeals (R. 60).

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred:

1. In holding that the taxpayers as trustees of the Boston Elevated Railway Company, having been appointed under a Special Act of the Massachusetts legislature, providing for public management and operation of the railway properties, were exercising essential governmental functions of the State and hence their salaries were exempt from Federal taxation.

2. In holding that the compensation received by the taxpayers as such trustees was not subject to the Federal income tax.

3. In holding invalid the provisions of Article 88 of Treasury Regulations 69.

4. In reversing the decision of the Board of Tax Appeals.

SUMMARY OF ARGUMENT

I

The statute imposes a tax upon the income of every individual derived from compensation for service and from all sources whatsoever. The court below held that the respondents, as trustees of the railway, exercised essential governmental functions of the Commonwealth of Massachusetts and accordingly, under the Treasury Regulations, their compensation was exempt from taxation. The court also held that regardless of the nature

of their functions the respondents were officers of the State and that their compensation as such officers was exempt from the Federal income tax.

The doctrine of implied constitutional immunity from taxation by the Federal Government of the agencies and instrumentalities employed by a State is limited to those exercising strictly governmental functions of the State. In determining the extent to which the doctrine applies, the reason for the rule must control and the exemption must depend finally upon the effect of the tax upon the exercise by the State of its essential functions of government, although consideration should also be given to the inherent nature of the agency, and its relation to government.

The respondents were trustees of the railway appointed under the Special Act of the Legislature of Massachusetts by which, upon acceptance by the company, the State took over the management and operation of the railway. The trustees were appointed solely for the purpose of managing and operating the railway and to the end that adequate transportation service might be maintained were authorized to fix rates of fare sufficient to meet the cost of service. Under the agreement, the State obligated itself to advance to the company any deficits incurred in the cost of operation, such deficits to be raised by taxation. Any sums advanced by the State, however, were to be repaid from any excess revenues realized from operation.

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It is no part of the essential governmental functions of a State to furnish means of transportation to its people. By assuming the management and operation of the railway the State of Massachusetts exercised no essential power of government but embarked upon a venture of a purely private character. When a State departs from the essential functions of government and engages in a business or activity of a purely private nature, it and the instrumentalities employed therein are subject to a nondiscriminatory tax imposed by the Federal Government. Since the assumption of the management and operation of the railway by the State was not a governmental power, it follows necessarily that the respondents as trustees were not agents or instrumentalities exercising essential powers of government of the State. Accordingly, the compensation received by the respondents as trustees, which compensation was paid by the company and not the State, is not within the appropriate scope of the doctrine of implied constitutional immunity and is subject to the Federal income tax.

II

The provisions of the regulations as to the compensation of "officers" are valid and are applicable in this case. The court below held that the trustees were officers of the State and that there is no basis for the requirement of the regulations that the compensation must be received for services

rendered in the exercise of governmental functions. In so holding, the court either ignored or overlooked explicit and well-known decisions of this Court. *Flint* v. *Stone Tracy Co.*, 220 U.S. 107; *South Carolina* v. *United States*, 199 U.S. 437; *Ohio* v. *Helvering*, 292 U.S. 360.

III

The fact that the respondents had the power to fix rates and to declare deficits which were used as a basis of taxation is not sufficient to exempt from taxation the salaries which they received for managing the railroad. The respondents had no discretion in fixing rates, and they had no power to levy taxes. Their authority with respect to each was merely ministerial.

Moreover, the compensation received by the respondents was not paid for the exercise of these powers. The salaries were paid to the trustees *by the company* and not by the Commonwealth, and they were paid for their services as managers of the company. If the respondents exercised any essential governmental powers, they received no compensation on that account; and their compensation received for other services is not exempt.

Even if the salary paid by the company could be regarded as paid in part as compensation for essential governmental powers exercised by the respondents on behalf of the State, it would not follow that the entire amount of the compensation would be

exempt from Federal tax. If it is necessary or proper to allocate the compensation actually received, the respondents must fail, for they have produced no evidence of the proper basis of allocation. The fact that such an allocation would be difficult to make does not furnish any basis for the respondents' contention that the entire salary should be exempt.

ARGUMENT

The Circuit Court of Appeals held that the taxpayers were public officers exercising essential governmental powers of the Commonwealth of Massachusetts and accordingly that their compensation is exempt from Federal income taxation under the Treasury Regulations. It was also held that in any event the Federal Government is without power to tax the compensation paid to the taxpayers as public officers of the Commonwealth, regardless of the nature of the functions they exercised. The petitioner contends that the taxpayers were agents or officers exercising a proprietary, and not a governmental, function of the State, and that their compensation is not exempt from Federal taxation either under the Treasury Regulations or under the principle of immunity of the instrumentalities of one government from taxation by another. The Special Act provided that in the management and operation of the railway the respondents should be deemed to be acting as

agents of the company and not of the Commonwealth and they were paid as such agents by the company for managing the railroad.

I

THE OPERATION OF A STREET RAILWAY SYSTEM IS NOT AN ESSENTIAL FUNCTION OF A STATE

The doctrine, resulting from our dual system of government, that the agencies, means, and instrumentalities through which a State exercises its essential governmental powers are immune from taxation by the Federal Government, and that those of the Nation are similarly exempt from state taxation, has long been established. *McCulloch* v. *Maryland,* 4 Wheat. 316; *Osborn* v. *Bank,* 9 Wheat. 738; *Dobbins* v. *Commissioners of Erie County,* 16 Pet. 435; *The Collector* v. *Day,* 11 Wall. 113; *United States* v. *Railroad Co.,* 17 Wall. 322; *Ambrosini* v. *United States,* 187 U.S. 1; *Indian Motocycle Co.* v. *United States,* 283 U.S. 570, 575. In *Fox Film Corp.* v. *Doyal,* 286 U.S. 123, 128, this Court, in pointing out that this principle of immunity from taxation has its inherent limitations, said:

> It is aimed at the protection of the operations of government (*McCulloch* v. *Maryland,* 4 Wheat. 316, 436), and the immunity does not extend "to anything lying outside or beyond governmental functions and their exertions." *Indian Motocycle Co.* v. *United States,* 283 U.S. 570, 576, 579.

> Where the immunity exists, it is absolute, resting upon an "entire absence of power" (*Johnson* v. *Maryland,* 254 U.S. 51, 55, 56), but it does not exist "where no direct burden is laid upon the governmental instrumentality, and there is only a remote, if any, influence upon the exercise of the functions of government" *Willcuts* v. *Bunn,* 282 U.S. 216, 225.

See also *Trinityfarm Co.* v. *Grosjean,* 291 U.S. 466, 472. As this Court said in *Willcuts* v. *Bunn, supra,* (p. 225):

> The limitation of this principle to its appropriate applications is also important to the successful working of our governmental system.

The immunity does not extend to every activity upon which a State may embark but is limited to those of a strictly governmental character. Only those instrumentalities through which the State *directly* and *immediately* exercises its essential powers of government are exempt from Federal taxation. *Metcalf & Eddy* v. *Mitchell,* 269 U.S. 514. Where the State engages in a business or performs acts of a private nature, it and the agencies through which it acts are subject to the power of taxation vested by the Constitution in Congress. *Ohio* v. *Helvering, supra; South Carolina* v. *United States, supra.*

In the *South Carolina* case, this Court held that since the State was not exempt from the tax, the taxing statute reached the individual sellers who

acted as dispensers for the State. So in the case at bar, even if the State had owned the railway company, the company would not have been exempt from taxation by the Federal Government. And certainly the fact that the State operated the railway under a lease arrangement, did not exempt the railway from Federal taxation, and as held in the *South Carolina* case, the statute likewise reached the individual trustees who acted in a sense for the State, but were in the language of the Special Act, the agents of the company and not of the Commonwealth. They cannot claim an exemption which their principal could not claim.

Here the railway company, a private corporation, was the instrumentality used by the State to operate the railroad. The State leased the railroad and the corporation continued in existence, its property was by the explicit provisions of the Special Act subject to taxation by the State, and also subject to suits for damages resulting from the negligence of the trustees and the other agents and employees of the company. The railway company continued to have a president and other officers, and a board of directors which was not removable by the board of trustees (Sec. 2).

Admittedly in the operation of the railroad, the State was not exercising any of its sovereign or essential powers of government, but embarked upon a private enterprise, and as the instrumentality was not immune from either State or Federal taxation, the compensation which the agents received from

the company for their services in managing and operating this private enterprise, is not immune from taxation. When the instrumentality is one which exercises an essential governmental function, the immunity extends not only to the instrumentality itself, but to income derived from it.

> When, however, the question is approached from the other end of the scale, it is apparent that not every person who uses his property or derives a profit, in his dealings with the government, may clothe himself with immunity from taxation on the theory that either he or his property is an instrumentality of government within the meaning of the rule.
>
> [*Metcalf & Eddy* v. *Mitchell, supra* (522).]

As this Court said in the *Indian Motocycle Co.* case, *supra* (p. 576)—

> Where a State departs from her usual governmental functions and "engages in a business which is of a private nature", no immunity arises in respect of her own or her agents' operations in that business.

It is doubtless impracticable to formulate any comprehensive rule for determining what agencies of a State are exempt from Federal taxation, especially in close cases falling between the two extremes of governmental and private operations where it is necessary to separate those activities having some relation to government which are subject to taxation from those which are exempt. The reason for the principle of immunity, how-

ever, must control its operation. Under our system the Federal Government must exercise its authority within the States, and while there may be no *undue* interference by one government with the exercise by the other of its powers, taxation by either necessarily and unavoidably has some effect upon the other. Accordingly, the doctrine of immunity of a State and its instrumentalities from taxation by the Federal Government calls for a practical test which allows the State to discharge its functions with a minimum of interference, and the principle must not be so extended as seriously to impair the taxing power of the Nation. While consideration should be given to the nature of the governmental agency in determining the question of tax exemption, the extent to which the doctrine is applicable depends finally upon the effect of the tax upon the State's essential powers of government. *Metcalf & Eddy* v. *Mitchell, supra* (pp. 522–524).

The obvious purpose of the special legislation was to substitute public operation and control of the railway for the private management and to fix rates of fare sufficient to meet the cost of service to the end that adequate service might be maintained. The State, however, did not substitute public ownership of the railway for private ownership. The railway remained the property of the company, a private corporation operated for private profit. The company has outstanding bonds and stocks and

the Special Act made it the duty of the trustees to pay the interest on the bonds and to pay dividends on both the preferred and common stock. (Secs. 3, 6, 11; *infra,* pp. 39, 42. See also Sec. 15, *infra,* p. 44.) It was expressly provided (Sec. 2, *infra,* p. 37) that in the exercise of the powers conferred the trustees should "be deemed to be acting as agents of the company and not of the commonwealth." While the State undertook to supply such funds as might be required by a deficiency in income to meet the cost of service, the Act provided for reimbursement of the State for any sums advanced (Sec. 11, *infra,* p. 42), and the State is to receive any surplus in the reserve fund at the termination of public operation (Sec. 13, *infra,* p. 43). It is plain that in thus providing for public *operation* of the railway the Commonwealth of Massachusetts was not exercising any essential governmental function, but was merely lending its aid to a private enterprise. True the railway was affected with a public interest, in that the facilities furnished for transportation were for the convenience and comfort of the people of the communities served by the railway. But the railway was not an instrumentality of government and the operation of the railway was not an essential governmental function or activity.

The Special Act under which the State assumed the operation of the railway through trustees, after acceptance by the company, was in effect a lease of the railway for an adequate consideration.

Opinion of the Justices, 231 Mass. 603, 609; *Boston* v. *Treasurer & Receiver General,* 237 Mass. 403, 413; *Opinion of the Justices,* 261 Mass. 523, 541. If the State had taken title to and acquired ownership of the railway company and its properties and operated the same it would not have thereby exercised any of the powers essential to government. Much less then can it be said that the mere operation of this public utility by the State through duly appointed agents under a lease is a discharge of any of the State's functions of Government.

This Court has said in unequivocal and unqualified terms, in considering taxation of public utility companies, that:

> It is no part of the essential governmental functions of a State to provide *means of transportation,* supply artificial light, water, and the like.
>
> These objects are often accomplished through the medium of private corporations, and, though the public may derive a benefit from such operations, the companies carrying on such enterprises are, nevertheless, private companies, whose business is prosecuted for private emolument and advantage. * * *
>
> The true distinction is between the attempted taxation of those operations of the States essential to the execution of its governmental functions, and which the State can only do itself, and those activities which are of a private character. The former, the United States may not interfere with by tax-

> ing the agencies of the State in carrying out its purposes; the latter, although regulated by the State, and exercising delegated authority, such as the right of eminent domain, are not removed from the field of legitimate Federal taxation. [*Flint* v. *Stone Tracy Co.*, *supra* (p. 172). (Italics ours.)]

As the assumption by the State of the management and operation of the railway was for public purposes, the State had the power to levy taxes for the purpose of maintaining this transportation service. *Boston* v. *Treasurer & Receiver General, supra; Boston* v. *Jackson,* 260 U.S. 309, 315. But the power exercised by the State to maintain this service for public purposes was not governmental. The terms "public purpose" and "governmental purpose" are not synonymous. *State of North Dakota* v. *Olson,* 33 F. (2d) 848, 852 (C.C.A. 8th), dismissed for want of jurisdiction, 280 U.S. 528; 2 Cooley, Taxation (4th ed.) Sec. 639.

The management and operation of the railway by the State was no less a private venture than the control of the liquor traffic by the States of Ohio and South Carolina through state-owned dispensaries and appointed agents. Ohio and South Carolina each took over control of the liquor traffic in furtherance of a state policy and for public purposes, for the general welfare and in the interest of the people of the State. Those States, however, and the agencies employed for such purposes were held subject to the Federal tax imposed upon per-

sons engaged in the liquor business, because, notwithstanding the public purpose served, the sale of liquor by the States was a private enterprise and not a function of government. *Ohio* v. *Helvering, supra; South Carolina* v. *United States, supra.* Similarly, notwithstanding the public purpose accomplished, the Commonwealth of Massachusetts by assuming the management and operation of the railway entered upon a purely private enterprise and was not exercising any of its ordinary powers of government.

Under the principle of the *Ohio* and *South Carolina* cases, had the State not only operated but also owned the railway, it would have been subject to a Federal tax upon that business. Indeed, the State itself recognized that it was not exercising any of its normal functions of government, for in Section 2 of the Act (*infra,* p. 37) it provided that the company and its stockholders should remain subject to taxation by the State and its subdivisions to the same extent as if the company managed and operated the railway. In *Boston Elevated R. Co.* v. *Malley,* 24 F. (2d) 758, 759 (Mass.), the court said:

> It would be a curious arrangement under which the corporation continued to be fully taxable as such for the benefit of the commonwealth, while it escaped taxation by the federal government.

See also *Group No. 1 Oil Corp.* v. *Bass,* 41 F. (2d) 483 (C.C.A. 5th), affirmed, 283 U.S. 279; *Wanless*

Iron Co. v. *Commissioner,* 29 B.T.A. 834. It was early determined that the company remained subject to Federal tax upon the business conducted, notwithstanding the absolute control of its properties by the State. *Boston Elevated R. Co.* v. *Malley,* 24 F. (2d) 758, 759 (Mass.); *Boston Elevated R. Co.* v. *Malley,* 288 Fed. 864 (Mass.). In the Act itself the State acknowledged that it was assuming the management and operation of a private business and did not regard such action as governmental.

It would seem to follow necessarily that the respondents as trustees of the railway were not essential governmental agencies or instrumentalities of the State. If, as the foregoing discussion seems to demonstrate, the State exercised no essential power of government in providing for the management and operation of the railway, then *a fortiori* the respondents as managers of the railway could not be agencies or instrumentalities exercising essential powers of government. Although the trustees were appointed under and their tenure and compensation were fixed by the Act, and they have been referred to as public officers, it is plain that they were not public officers in the sense of performing governmental duties. The Act provided that they should "not be considered public officers" for certain purposes (sec. 1) and as has been pointed out, the Act itself expressly declared that in the management and operation of the railway the trustees should be deemed to be acting as agents

of the company and not of the State. Section 2; *infra,* p. 37. The trustees were appointed for the purpose of managing and operating the railway; all contracts entered into and all acts performed by them were executed in the name of and on behalf of the company. At the most the trustees were the agents through which the State managed and operated the railway, a purely private business, and were not in anywise governmental instrumentalities of the State.

The tax imposed upon the compensation received by the respondents as trustees placed no burden upon the Commonwealth of Massachusetts. Although the salary of the trustees was fixed by the Special Act, the agreement between the State and the company, it was expressly provided that the compensation of the trustees should be paid by the company. See Section 1, *infra,* p. 36. The salary of the trustees was not paid by the State, and the Federal tax upon such income in nowise interfered with or affected the State in the establishment of agencies for the execution of its powers of government. It is true that under the agreement the State was obligated to advance the company any deficits incurred in operations, and for 1919 nearly $4,000,000 was paid by the State pursuant to the agreement. But, as the court below recognized, the amount so advanced was a debt of the company to the State, and it was contemplated that all sums advanced by the State to make up deficits should

be repaid. Moreover, there is nothing in the record to indicate that the company operated at a deficit during the years here involved (1926 to 1929, inclusive) or in any year other than 1919.[1] There is consequently no warrant for saying that the salaries of the respondents as trustees for the years in question were not paid by the company and the company alone.

The burden of the tax here in question falls solely upon the respondents individually. The Commonwealth of Massachusetts is not affected by the tax even indirectly, and certainly the taxation of the individual incomes of the respondents is not a direct interference with the exercise of any of the governmental powers of the State. It cannot be said that the imposition of this tax in anywise restricts the State in the full and free exercise of its sovereign governmental powers or lessens the power of the State to employ agencies or instrumentalities to execute its governmental powers. See *Miller* v. *McCaughn*, 27 F. (2d) 128 (C.C.A. 3d). Since, as this Court held in *Metcalf & Eddy* v. *Mitchell*, *supra*, the reason for the doctrine of implied immunity must be the guiding principle in determining its proper application, it seems clear that the

[1] The annual reports of the trustees for the years 1926 to 1929, inclusive, show that only in the year 1919 was any deficit incurred by the company which the State was called upon to pay. And the report for 1929 (p. 35) shows that prior to that year $2,630,818.32 of the advance for 1919 had been repaid to the State.

compensation received from the railway company by the respondents appointed to manage and operate the railroad as trustees is not within the appropriate scope of the rule of exemption and is subject to the Federal income tax.

The Circuit Court of Appeals recognized that by "classical standards" (R. 59) the management and operation of the railroad by the State was not an exercise of its essential powers of government, but questioned how long such standards would prevail in view of the tendency of government to extend its field of activity. In so doing, we submit, the court below has confused two wholly different questions: (1) the activities in which a State may engage if it chooses, and (2) the extent to which the State will be immune from Federal taxation if it engages in those activities. It was the very tendency to give a broad answer to the first of these questions which this Court relied on in *South Carolina v. United States, supra,* as requiring the limitation of immunity from taxation to those agencies and instrumentalities and activities of the State which are of a *strictly governmental* character. That this Court does not deem the expansion of the activities of government a justification for departing from "classical standards" in determining immunity from taxation, but rather considers such tendency as the imperative necessity for confining the doctrine of immunity within appropriate bounds and applying it only to those agencies through which

the State *directly* and *immediately* exercises powers of a strictly *governmental* character, is manifest from the recent decision in *Ohio* v. *Helvering, supra.*

Similar results have been reached in deciding closely related questions. Upon the authority of *Metcalf & Eddy* v. *Mitchell, supra,* this Court recently reversed *per curiam* two decisions of Circuit Courts of Appeals which held the compensation of an attorney employed by a State in special litigation and the compensation of an attorney employed by a municipality exempt from the Federal income tax. *Lucas v. Reed,* 281 U.S. 699; *Lucas* v. *Howard,* 280 U.S. 526. Those decisions have served largely to put at rest questions of the taxability of income received by a taxpayer from a State for services as special counsel or the like. See, e.g., *Burnet* v. *McDonough,* 46 F. (2d) 944 (C.C.A. 8th); *Lewis* v. *Commissioner,* 47 F. (2d) 32 (C.C.A. 3d); *Haight* v. *Commissioner,* 52 F. (2d) 779 (C.C.A. 7th), certiorari denied, 285 U.S. 537; *Register* v. *Commissioner,* 69 F. (2d) 607 (C.C.A. 5th). Similarly, in this case the respondents, although appointed by the Executive for specified terms, were not agencies created by the State to enable the State to perform a governmental function, but on the contrary they were appointed trustees to manage and operate the railroad, a nongovernmental activity, and were paid by the Railway Company; and their compensation received from the railway company is not exempt.

Two cases which seem contrary to our contentions should be referred to. In *Frey* v. *Woodworth,* 2 F. (2d) 725 (Mich.), it was held that the operation by a city of a municipally owned street railway was a governmental function and the compensation of an employee of the railway company was held to be exempt from Federal taxation. In *United States* v. *King County, Wash.,* 281 Fed. 686 (C.C.A. 9th), it was held that the operation of a county owned ferry was a governmental function and exempt from the Federal excise tax. In the light of the authorities referred to above, these cases, we submit, are unsound and cannot be deemed authoritative. In the *Woodworth* case, a writ of error taken by the Collector was dismissed on his motion (270 U.S. 669) for the reason that subsequent to the decision of the lower court the Revenue Act of 1926 was passed, providing in Section 1211 that "any taxes imposed by the Revenue Act of 1924 or prior revenue Acts upon any individual in respect of amounts received by him as compensation for personal services as an officer or employee of any State or political subdivision thereof * * * shall * * * be abated, credited, or refunded." No such statutory provision is applicable for the taxable years 1926 to 1929 inclusive here involved. *Commissioner* v. *Ogden,* 62 F. (2d) 334 (C.C.A. 1st), and *Jamestown & Newport Ferry Co.* v. *Commissioner,* 41 F. (2d) 920 (C.C.A. 1st), likewise rested upon express statutory exemptions.

II

THE PROVISIONS OF THE REGULATIONS AS TO THE COMPENSATION OF "OFFICERS" ARE VALID AND ARE APPLICABLE TO THIS CASE

Article 88 of Regulations 69 (*infra*, p. 35), promulgated under the 1926 Revenue Act, provides that the compensation paid to officers and employees of a State is exempt from income taxation only if received for services "rendered in connection with the exercise of an essential governmental function." Article 643 of Regulations 74 and 77, promulgated under succeeding Revenue Acts, is the same. Accordingly, the regulation has received the approval of Congress through reenactment of the statutory provisions upon which it is based. *United States* v. *Dakota-Montana Oil Co.*, 288 U.S. 459, 466. The regulation is plainly consistent with the statute, and we submit that it is a proper expression of the appropriate scope of the implied constitutional immunity of a State and its agencies from Federal taxation.

The court below, however, held that the trustees were officers of the State and that there is no basis for the requirement of the regulations that the compensation must be received for services rendered in the exercise of governmental functions (R. 59–60). In so holding the court either ignored or overlooked explicit and well-known decisions of this Court. The distinction made by the regu-

lations between state officers and employees exercising governmental powers and those employed by the State in carrying on some private venture for the public good is based upon principles established by this Court in *Flint* v. *Stone Tracy Co., supra, South Carolina* v. *United States, supra,* and *Ohio* v. *Helvering, supra.*

It is plain from decisions of this Court and the lower Federal courts, as shown earlier in this brief, that only the agencies and instrumentalities of the State exercising essential functions of government are exempt from Federal taxation, and when the State engages in a private business both the State and the agencies it employs are subject to the taxing power of the Nation. Hence, the mere fact that the respondents, as trustees of the railway, were appointed by the State to serve as managers of the railway for 10 years is not sufficient to render their compensation immune from the nondiscriminatory Federal tax imposed upon the net income of every individual. Especially is this true, when the Act says they shall be deemed the agents of the railway company and paid by it. As trustees the respondents were no more than the agencies through which the State carried out its undertaking to manage and operate the railway. But the management and operation of the railway were no part of the functions of *government* of the Commonwealth of Massachusetts. Necessarily, therefore, the trustees exercised no governmental powers and were not

such agencies or instrumentalities of the State as are exempt from Federal taxation under any proper application of implied constitutional immunity.

The court below quoted only a portion of a sentence from the opinion of this Court in *Metcalf & Eddy* v. *Mitchell, supra* (p. 524), in support of the holding that an officer of either a State or the Nation is exempt from taxation by the other irrespective of the services performed or the nature of his employment. The complete sentence from which the quotation was taken is "any taxation by one government of the salary of an officer of the other, or the public securities of the other, or an agency created and controlled by the other, *exclusively to enable it to perform a governmental function* * * * is prohibited." (Italics ours.) The court below, in reproducing this sentence, omitted the words which we have italicized.

Nor does the holding of the court below receive any support from *Dobbins* v. *Commissioners of Erie County, supra,* and *The Collector* v. *Day, supra,* which were also cited. In the *Dobbins* case, Pennsylvania sought to tax the office, valued according to the salary, of a captain in the Federal Revenue Cutter Service. The tax was held invalid on the ground that an officer of the Revenue Cutter Service is an agency employed in the exercise of sovereign governmental powers of the Nation, namely, taxation and the regulation of interstate and foreign commerce. In the *Day* case, the Federal Govern-

ment sought to tax the salary of the judge of the Court of Probate and Insolvency for the County of Barnstable, Massachusetts. It was held that the Federal Government could not tax the salary of a *judicial* officer of the State for the reason that the judicial department is one of the sovereign rights and powers of the State and a judge is an instrumentality through which the State exercises such powers. In both the *Dobbins* and *Day* cases the officer whose salary was held immune from taxation was exercising essential governmental powers.

III

THE FACT THAT THE RESPONDENTS HAD THE POWER TO FIX RATES AND TO DECLARE DEFICITS WHICH WERE USED AS A BASIS OF TAXATION IS NOT SUFFICIENT TO EXEMPT FROM TAXATION THE SALARIES WHICH THEY RECEIVED FOR MANAGING THE RAILROAD

The respondents in their brief in opposition laid great stress on the fact that under the Special Act of Massachusetts they had the power to fix rates, and to declare deficits, which, upon certification to the proper officers of the Commonwealth, became the basis for the levy of taxes from the communities affected. We submit that the possession of these powers does not form an adequate basis for the decision below.

The basis upon which the rates were to be fixed was provided for in detail in the Act itself. See Secs. 6–11 (*infra*, pp. 39–42). Cf. *Cleveland Railway Co.* v. *Commissioner*, 36 F. (2d) 347 (C.C.A. 6th), certiorari denied, 281 U.S. 743. The trustees

were given substantially no discretion, and were not required to make determinations on questions involving the exercise of judgment, such as the valuation of the property. The trustees had no power to levy taxes. They could only certify the amount of any deficit to the Treasurer and Receiver General of the Commonwealth, a mere ministerial act.

The authority conferred upon the trustees in this respect was essentially the same as the authority conferred upon the company itself when private operation should be resumed. Sec. 15 of the Special Act (*infra,* p. 44).

Moreover, even if these powers could be considered as the exercise of essential powers of *government,* it would seem clearly not to follow that the salaries paid to the respondents would be exempt. The salaries were paid to the trustees *by the company* for their services as managers of the company and as agents of the company. This is made plain by the provision of the Act that "in the management and operation" of the company they "shall be deemed to be acting as agents of the company and not of the commonwealth." The salaries involved in this case were paid by the company, and it would seem to be clear that they were paid by the company as compensation for the services rendered by the respondents to the company. If the respondents exercised any essential governmental powers, they received no compensation on that account; and their compensation received for

managing the railroad can be no more exempt from taxation than would the private income of an individual be exempt because he was also a state judge.

In *Flint* v. *Stone Tracy Co., supra* (p. 152), this Court pointed out that in the cases where a state tax had been held invalid—

> the decision rested upon the proposition that the corporation was created to carry into effect powers conferred upon the Federal Government in its sovereign capacity, and the attempted taxation was an interference with the effectual exercise of such powers.

This Court in that case further said:

> In *Osborn* v. *The Bank, supra,* a leading case upon the subject, whilst it was held that the Bank of the United States was not a private corporation, but a public one, created for national purposes, and therefore beyond the taxing power of the State, Chief Justice Marshall, in delivering the opinion of the court, conceded that if the corporation had been originated for the management of an individual concern, with private trade and profit for its great end and principal object, it might be taxed by the State. Said the Chief Justice (p. 359):
>
> "If these premises [that the corporation was one of private character] were true, the conclusion drawn from them would be inevitable. This mere private corporation, engaged in its own business, with its own views, would certainly be subject to the tax-

> ing power of the State, as any individual would be; and the casual circumstance of its being employed by the Government in the transaction of its fiscal affairs would no more exempt its private business from the operation of that power than it would exempt the private business of any individual employed in the same manner."

Even if the salary paid by the company could be regarded as paid in part as compensation for the powers exercised by the respondents on behalf of the State, it would not follow that the entire amount of the compensation would be exempt from Federal tax. Certainly the major part of the respondents' services were rendered on behalf of the company and their compensation for those services would not be exempt. If it is necessary or proper to allocate the compensation actually received between the two types of services (which we deny), then the respondents' case must likewise fail; for the burden of proof was on them, and they have produced no evidence of the proper basis of allocation. *Reinecke* v. *Spalding,* 280 U.S. 227. The fact that such an allocation would be difficult, or perhaps impossible, to make does not furnish any basis for the respondents' contention that the entire salary should be exempt. *Burnet* v. *Houston,* 283 U.S. 223.

CONCLUSION

The instant case presents a striking instance of that necessity observed by the Court in *South Caro-*

lina v. *United States, supra,* for confining the doctrine of implied constitutional immunity within appropriate bounds and limiting its application to those agencies which are of a strictly governmental character. The management and operation of the railway was not an essential governmental activity of the Commonwealth of Massachusetts, and the respondents as trustees, were not officers, agencies, or instrumentalities exercising essential powers of government. A tax upon the compensation received by the respondents, which was paid by the company and not by the State, imposed no burden upon the State and in no degree interfered with the free and unrestricted power of the State to employ agencies exclusively for the discharge of its strictly governmental functions. It would seem clear, therefore, that the doctrine of implied constitutional immunity is not applicable here and the compensation received by the respondents is subject to the Federal income tax.

We respectfully submit that the decision of the court below is erroneous and should be reversed.

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SEPTEMBER 1934.

APPENDIX A

Revenue Act of 1926, c. 27, 44 Stat. 9:

SEC. 212. (a) In the case of an individual the term "net income" means the gross income as defined in section 213, less the deductions allowed by sections 214 and 206.

* * * * *

(U.S.C. App., Title 26, Sec. 953.)

SEC. 213. For the purposes of this title, except as otherwise provided in section 233—

(a) The term "gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service * * * of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property * * * or gains or profits and income derived from any source whatever. The amount of all such items shall be included in the gross income for the taxable year in which received by the taxpayer, unless, under methods of accounting permitted under subdivision (b) of section 212, any such amounts are to be properly accounted for as of a different period.

* * * * *

(U.S.C. App., Title 26, Sec. 954.)

Revenue Act of 1928, c. 852, 45 Stat. 791, 797:

Sections 21 and 22 (a) of the Revenue Act of 1928, so far as material, are substantially the same as

Sections 212 (a) and 213 (a), respectively, of the Revenue Act of 1926, as set forth above.

Treasury Regulations 69, promulgated under the Revenue Act of 1926:

> ART. 88. *Compensation of State officers and employees.*—Compensation paid to its officers and employees by a State or political subdivision thereof for services rendered in connection with the exercise of an essential governmental function of the State or political subdivision, including fees received by notaries public commissioned by States and the commissions of receivers appointed by State courts, is not taxable. Compensation received for services rendered to a State or political subdivision thereof is included in gross income unless (*a*) the person receives such compensation as an officer or employee of a State or political subdivision, and (*b*) the services are rendered in connection with the exercise of an essential governmental function. But see section 1211 as to 1924 and prior years.

Article 643 of Treasury Regulations 74 and 77, promulgated under the Revenue Acts of 1928 and 1932, so far as material, is substantially the same as Article 88 of Regulations 69, set forth above.

APPENDIX B

Massachusetts, Special Acts and Resolves, 1918:

CHAP. 159. AN ACT TO PROVIDE FOR THE PUBLIC OPERATION OF THE BOSTON ELEVATED RAILWAY COMPANY

Be it enacted, etc., as follows:

SECTION 1. The board of trustees of the Boston Elevated Railway Company is hereby created, to consist of five persons to be appointed by the governor, with the advice and consent of the council. The persons so appointed shall be sworn before entering upon the performance of their duties; shall own no stock or other securities of the Boston Elevated Railway Company or of any company owned, leased or operated by it; shall serve for the term of ten years from the date when they assume the management of the company as hereinafter provided and until their successors are duly appointed and qualified, and each shall receive from the company as compensation for his services five thousand dollars annually. In case of any vacancy in said board by reason of death, resignation, or otherwise, the governor, by and with the consent of the council, shall fill the vacancy. The board shall designate one of the trustees so appointed to serve as chairman. Any member of the board may be removed for cause by the governor, with the advice and consent of the council.

Said trustees shall not be considered public officers within the meaning of section twenty-five of chapter five hundred and fourteen of the acts of nineteen hundred and nine, but shall be subject in all other respects to the provisions of said section to the same extent as are the directors of the Boston Elevated Railway Company, but said section shall not apply to recommendations by the governor to said trustees. The provisions of section one of chapter seven of the Revised Laws shall not apply to the said board.

If the public management and operation of the railway system of the Boston Elevated Railway Company shall continue beyond the original period of ten years the governor shall, with the advice and consent of the council, at the expiration of each ten-year period during the continuance of public management and operation, appoint five successor trustees to serve for a period of ten years and until their successors are appointed and qualified, but not exceeding the period of public management and operation. Said trustees shall assume the management and operation of the company's property on the first day of the month next following their appointment and qualification.

SEC. 2. Said board of trustees, hereinafter called the trustees, shall manage and operate the Boston Elevated Railway Company hereinafter called the company, and the properties owned, leased, or operated by it, for a period of ten years, commencing on the first day of the month next after their appointment and qualification, and, subject to the provisions of this act, shall take and have possession of said properties in behalf of the commonwealth during the period of public

operation, and, for the purposes of this act, shall, except as is otherwise provided in this act have and may exercise all the rights and powers of said company and its directors, and, upon behalf of said company, shall receive and disburse its income and funds. They shall have the right to appoint and remove in their discretion the president, treasurer, and clerk of the corporation, and all officers of the company other than the board of directors. They shall have the right to regulate and fix fares, including the issue, granting and withdrawal of transfers, and the imposition of charges therefor, and shall determine the character and extent of the service and facilities to be furnished, and in these respects their authority shall be exclusive and shall not be subject to the approval, control, or direction of any other state board or commission.

In the management and operation of the said company and of the properties owned, leased, or operated by it, as authorized by this act, the trustees and their agents, servants, and employees shall be deemed to be acting as agents of the company and not of the commonwealth, and the company shall be liable for their acts and negligence in such management and operation to the same extent as if they were in the immediate employ of the company, but said trustees shall not be personally liable. A majority of the board shall constitute a quorum for the transaction of business, and the action of a majority of those present at any meeting shall be deemed the action of the trustees.

Nothing herein contained shall be held to affect the right of the commonwealth or any subdivision thereof to tax the company or its stockholders in the same manner and to

the same extent as if the company had continued to manage and operate its own property.

SEC. 3. The trustees shall have authority to make contracts in the name and on behalf of, and to issue stocks, bonds, and other evidences of indebtedness of, the company. * * * The trustees shall cause to be paid all amounts which may from time to time become due from the company, and shall declare dividends at the appointed times upon the preferred and common stock of the company, and provide for the payment of the same.

* * * * *

SEC. 5. The Boston Elevated Railway Company shall, prior to or at the time of its acceptance of this act, provide for raising three million dollars in cash by the issue of preferred stock at not less than the par value which shall be one hundred dollars per share. * * *

One million dollars shall be set aside as a reserve fund to be used only for the purposes hereinafter specified, and the remaining two million dollars shall be subject to the disposition of the trustees to pay for the cost of additions and improvements to the company's property.

SEC. 6. The trustees shall from time to time, in the manner hereinafter provided, fix such rates of fare as will reasonably insure sufficient income to meet the cost of the service, which shall include operating expenses, taxes, rentals, interest on all indebtedness, such allowance as they may deem necessary or advisable, for depreciation of property and for obsolescence and losses in respect to property sold, destroyed, or abandoned, all other expenditures and charges which under the laws of the commonwealth

now or hereafter in effect may be properly chargeable against income or surplus, fixed dividends on all preferred stock of the company from time to time outstanding, and dividends on the common stock of the company from time to time outstanding at the rate of five percent per annum on the par value thereof during the first two years, five and one-half percent per annum on the par value thereof during the next two years and six percent per annum on the par value thereof during the balance of the period of public operation. * * *

SEC. 7. The trustees shall, within sixty days after their appointment and qualification, fix and put in operation rates of fare which in their judgment will produce sufficient income to meet the cost of the service as defined in section six, and within sixty days thereafter shall adopt and publish a schedule of eight different grades of fare, of which four shall be below and four above the rate of fare first established; and whenever by reason of any change in the existing rate of fare there are less than four grades, either above or below the rate then in force, the trustees shall forthwith adopt and publish a schedule of additional grades of fare so that there shall always be not less than four grades of fare above and below the existing rate of fare.

If at any time the trustees shall be of opinion that said rates of fare or schedule should be changed, either with regard to the method or basis upon which the fares and transfer privileges are established, or because the steps between the different grades are too small or too great, or for any other reason, the trustees may adopt, publish, and put in effect new schedules or rates of fare to take

the place of the existing schedule or rates of fare.

SEC. 8. The reserve fund shall be used only for the purpose of making good any deficiency in income as provided in section nine or for reimbursing the commonwealth as provided in sections eleven and thirteen, and until such use, may be invested in income-producing securities in the discretion of the trustees, and all income or interest received thereon shall be treated as part of the general income of the company.

SEC. 9. Whenever the income of the company is insufficient to meet the cost of the service as herein defined, the reserve fund shall be used as far as necessary to make up such deficiency, and whenever, on the other hand, such income is more than sufficient to meet the cost of the service, the excess shall be transferred to and become a part of the reserve fund.

SEC. 10. If, as of the last day of June in the year nineteen hundred and nineteen, or the last day of any September, December, March, or June thereafter, the amount of the reserve fund shall exceed by thirty percent or more the amount originally established, and during the preceding three months the income shall have exceeded the cost of the service, the trustees shall within one month thereafter put into effect the next lower grade of fare that has been adopted as provided in section seven; and if, as of any such last day of June, September, December, or March, the amount of the reserve fund shall be less than seventy percent of the amount originally established and during the preceding three months the income has been less than the cost of the service, the trustees shall within one month thereafter put into effect the next higher grade of fare, and the

fare shall continue to be decreased or increased, as the case may be, subject to the same conditions, if the amount of the reserve fund is above or below said limits, as of such quarterly dates. In determining the amount of the reserve fund for the purposes of this section only there shall first be deducted therefrom any amounts which have been paid by the commonwealth to the company under the provisions of section eleven, and for which the commonwealth has not been reimbursed.

SEC. 11. If, as of the last day of June in the year nineteen hundred and nineteen, or the last day of any December or June thereafter, the amount remaining in the reserve fund shall be insufficient to meet the deficiency mentioned in section nine, it shall be the duty of the trustees to notify the treasurer and receiver general of the commonwealth of the amount of such deficiency, less the amount, if any, in the reserve fund applicable thereto, and the commonwealth shall thereupon pay over to the company the amount so ascertained. Pending such payment it shall be the duty of the trustees to borrow such amount of money as may be necessary to enable them to make all payments, including dividend payments, as they become due. If, as of the last day of any June or December thereafter during the period of public operation, the reserve fund shall exceed the amount originally established, the trustees shall apply the excess, so far as necessary, to reimbursing the commonwealth for any amounts which it may have paid to the company under the provisions hereof, and the commonwealth shall thereupon distribute the amount so received among the cities and towns in which the company operates, in proportion to the

amounts which they have respectively been assessed as provided in section fourteen.

In order to meet any payment required of the commonwealth under the provisions of this section the treasurer and receiver general may borrow at any time, in anticipation of the assessments to be levied upon the cities and towns, such sums of money as may be necessary to make said payments, and he shall repay any sums so borrowed as soon after said assessments are paid as is expedient.

* * * * *

SEC. 13. It shall be the duty of the trustees to maintain the property of the company in good operating condition and to make such provision for depreciation, obsolescence and rehabilitation, that, upon the expiration of the period of public management and operation, the property shall be in good operating condition. If the period of public management and operation expires, control of the property shall then revert to the company, and if at that time the reserve fund shall be less than the amount originally established because the income during the period of public management and operation has been insufficient to pay the cost of the service, the commonwealth shall forthwith pay over to the company an amount sufficient to restore it to its original amount; and if the amount in said reserve fund is then in excess of the amount originally established and any amount required to meet the cost of the service to the expiration of such period, such excess shall be paid into the treasury of the commonwealth and distributed among the cities and towns in which the company operates in the same proportions as the assessments provided for by section fourteen.

SEC. 14. In case the commonwealth shall be called upon to pay to the trustees or the company any amount under the provisions of sections eleven and thirteen, such amount with interest or other charges incurred in borrowing money for the purpose shall be assessed upon the cities and towns in which the company operates by an addition to the state tax next thereafter assessed in proportion to the number of persons in said cities and towns using the service of the company at the time of said payment, said proportion to be determined and reported to the treasurer and receiver general by the trustees from computations made in their discretion for the purpose.

SEC. 15. Upon the termination of the period of public management and operation, the company shall manage and operate the property and may fix and collect such just and reasonable fares as will produce an income sufficient to pay the reasonable cost of the service as defined in section six, including dividends upon the common stock from time to time outstanding of six percent per annum on the par value thereof but no more, and may establish schedules of fares which shall automatically increase or decrease in the same manner as is authorized in the case of the trustees: *Provided,* that the commonwealth shall be under no liability to make any payments to the company by reason of any deficiencies in income accruing after the discontinuance of public operation. The company shall thereafter be subject to public regulation and supervision in such manner as may be determined by the general court, but such regulation and supervision shall not be exercised so as to reduce the income below

the reasonable cost of the service as defined in this act.

* * * * *

SEC. 18. With the exception of section five, which shall take effect upon the passage of this act, this act shall take effect upon its acceptance by the holders of not less than a majority of all the stock of the Boston Elevated Railway Company and by the holders of not less than a majority of all the stock of the West End Street Railway Company, given at meetings called for the purpose, and the filing of certificates of acceptances with the secretary of the commonwealth, and the filing with the said secretary of a certificate, signed and sworn to by a majority of the directors of the Boston Elevated Railway Company, that the entire three million dollars of preferred stock provided for by section five has been subscribed for, and at least thirty percent of his subscription has been paid in in cash by each subscriber, and that no dividends have been declared or paid upon the company's common stock since the passage of this act.

* * * * *

U. S. GOVERNMENT PRINTING OFFICE: 1934

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In the Supreme Court of the United States

OCTOBER TERM, 1933

No. 946

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

vs.

LELAND POWERS, EXECUTOR, ET AL.

RESPONDENTS' BRIEF OPPOSING PETITION FOR WRIT OF CERTIORARI

I. JURISDICTION OF THIS COURT.

The jurisdiction of this Court is invoked by the petitioner under Section 240(a) of the Judicial Code as amended by the Act of February 13, 1925. The respondents contend that there is not presented an appropriate case for the exercise of that jurisdiction; with particular reference to the principles embodied in paragraph 5 of Rule 38 of this Court.

II. STATEMENT.

The bulk of the petitioner's statement purports to be a summary of "the facts as found by the Board of Tax Appeals" (page 2 of petition) but in fact most of it is the petitioner's own resume of the terms of a Massachusetts statute, which was quoted from verbatim by the Board (compare pages 3 to 5 of the petition with

pages 24 to 29 of the record). The Board, whose decision the Circuit Court of Appeals reversed, made its own selections from the statute and supplied italics to represent its own point of view. The petitioner's resume of these selections is not unfair, but, as will be seen below, *does not fully present the picture from the point of view of the respondents and of the Circuit Court of Appeals.*

It may be helpful to present a summary of the decision of the Circuit Court of Appeals, reported in 68 F. (2nd) 634. (References are made to the pages of the record whereat the opinion is reprinted.) The Circuit Court of Appeals held in brief as follows:

A. The Commonwealth of Massachusetts took over the Boston Elevated Railway Co. under an "unusual arrangement," whereby the Railway Company, for a consideration, turned its property over to the Commonwealth for a term of years to be managed by Public Officials,—the respondents and their co-trustees. (Pages 81-2 of record.)

B. The respondents are public officers of the State. (Pages 82-3 of record.)

C. Concededly, the operation of a street railway is not, "by classical standards," an essential function of government. (Page 83 of record.)

D. The respondents, however, among their statutory powers, were invested with powers to fix the rates of a public utility and to direct the incidence of public taxation; both of which are "by any standard essentially governmental." (Page 83 of record.)

E. Regulations 69 Article 88 does not call for an arbitrary apportionment of a salary, between

governmental and non-governmental activities; and no such contention is made. (Page 83 of record; regulation at page 82 of record.)

F. The salaries of the respondents were therefore exempt from the Federal Income Tax even under the Treasury Department's own regulations, as properly construed. (Page 83 of record.)

G. *Also,* the salaries were not taxable on broader grounds, for they represented the compensation of officers of a state, which is constitutionally exempt from Federal taxation; and as to such compensation there is no precedent for discrimination according to the presence or absence of "an essential governmental function," nor yet for discrimination according to the immediate source of the payment of the compensation. (Pages 83-4 of record.)

Propositions A to F above assert that the respondents' salaries were not taxable, even under the regulation; and thus, of course, do not involve any decision whether the regulation, properly construed, has unduly attempted to narrow the scope of the constitutional principle of exemption.

Proposition G above asserts in effect that the respondent's compensation could not constitutionally be taxed and that *if* the regulation, properly construed, should be deemed to require a different conclusion, the regulation would then be in conflict with the underlying constitutional principle.

III. Relevant Statutes.

No relevant portion of any applicable Revenue Act contains any reference to the constitutional principle of exemption which is involved.

The Treasury regulation which purports to define and circumscribe the constitutional principle is set out in the petition at page 16 and in the decision of the Circuit Court of Appeals (page 82 of record).

Certain portions of the Massachusetts Special Acts 1918, c. 159, by which the respondents' offices were created and their duties delineated, are set out at page 15 infra as an Appendix, and there is indicated by italics the bearing of portions thereof upon the respondents' contentions.

IV. Argument.

We contend that the decision of the present case in the Circuit Court of Appeals presents no issue which this Court will care to bring up for discussion on certiorari.

The actual decision in the case is summarized under headings A to F at page 2, supra. What the court has done has been to apply, in a unique situation not likely to be paralleled closely in other instances, the simple and long established rule that neither the federal nor the state government can tax the compensation of the public officers of the other.

> *Buffington* v. *Day,* 11 Wall. 113.
> *Dobbins* v. *Commissioners,* 16 Pet. 435.
> *Metcalf* v. *Mitchell,* 269 U. S. 514.
> *Willcuts* v. *Bunn,* 282 U. S. 216, 225-6.
> *Indian Motocycle Co.* v. *United States,* 283 U. S. 570, 577.

In so doing, it has not had to touch at all upon the constitutionality of any statute; and it has not neces-

sarily invalidated any regulation of the Treasury Department, for in this particular case the public officers in question were primary officers of the state, deriving their authority directly from legislative enactment, and entrusted with a portion, sufficiently extensive to be significant, of the state's power over the rates and practices of public utilities and of the vital taxing power (page 83 of record; and Appendix, infra, pages 15, 16, 20-21).

The Circuit Court of Appeals has also said, however, that since the respondents were public officers it would not matter whether they performed "classical governmental functions" (pages 83-4 of record). We contend that there is no occasion to review the merits of this branch of the opinion; but we also point out that it is essentially a dictum, the altering of which should not affect the actual outcome of the case.

The petitioner has not reflected these distinctions in his petition; neither has he clearly adverted to the typical instances for the exercise of jurisdiction set out in subparagraph (b) of paragraph 5 of Rule 38 of this Court.

Nevertheless we proceed to answer his contentions in the order of their presentation.

1. The decision is not in conflict with

(a) *Flint* v. *Stone Tracy Co.*, 220 U. S. 107, involving a corporation *excise tax* upon a state chartered, but privately owned and operated, public utility corporation; or

(b) *South Carolina* v. *United States*, 199 U. S. 437, involving a *license tax* imposed upon dealers

in intoxicating liquors and held applicable to individual dispensers at state dispensaries "because they were the actual sellers," but not involving any tax upon *compensation* of public officers or employees; or

(c) *North Dakota* v. *Olsen,* 33 Fed. (2nd) 848, involving a *capital stock tax* on a bank incorporated by the state and the capital stock of which was owned by the state.

The petitioner does not remark the essential differences, both in the type of tax and in the subject of the taxation, between these cases and the present case. Thus he overemphasizes differences in language and neglects differences in substantive issues, failing to bear in mind that a particular issue will frequently invoke the use of language which cannot be literally applied in another case upon a different issue.

2. The decision did not necessarily hold the regulation invalid.

The petition does not anywhere, except perhaps by implication at page 9, challenge the holding that the respondents were public officers (pages 82-3 of record).

The court below held that the respondents had some important functions of the most essential governmental character (page 83 of record). This holding the petition challenges, although but feebly, at page 11.

The court held that the regulation did not mean that a salary was to be split artificially and allocated as between services of governmental and non-governmental character (page 83 of record). This the petition challenges not at all.

Thus the particular case was held to be within the regulation as well as within the constitutional exemption; and the actual decision of the case is hardly attacked at all by the petition and fails to present the possibility of any serious conflict, upon an important question, with the decisions of this Court or of other Circuit Courts of Appeal (or of the courts of Massachusetts, to no decision of which does the petition refer).

The petition makes something (at page 9) of the point that the compensation was not paid directly by the Commonwealth. But the regulation (page 7-8 of petition) does not clearly evoke this issue (compare the first sentence with the second sentence thereof) and the holding of the court below was correct. See page 9 of this brief, infra.

United States v. *Dakota-Montana Oil Co.* 288 U .S. 459, 466 is without bearing upon the present case, for

(a) The issue there turned upon statutory and not upon constitutional law.

(b) Neither a statute nor a regulation can alter or circumscribe the constitutional principle in the present case.

(c) The Revenue Acts do not even try to deal with this principle of exemption at all, and their re-enactment can hardly do more, despite the fact of the Department having tried to deal with the subject by regulation.

In the second branch of the decision, the court below did deny precedent for the discrimination set up in the regulation. The petitioner says what the discrimina-

tion "of course" was, but neglects to point out that what the court denied was the validity of the discrimination *as applied to the compensation of a public officer,* for which neither *South Carolina* v. *United States, supra,* nor *Flint* v. *Stone Tracy Co., supra,* is any authority.

Blair v. *Byers,* 35 Fed. (2nd) 326, involved an income tax upon the annual retainer received by an attorney from a city Board of Water Works Trustees. In that case it was held that the operation of waterworks is a proprietary and not a governmental function; but it was also held that the taxpayer was not a public officer or even an employee, and the years involved were 1920 to 1923 which are governed by Section 1211 of the Revenue Act of 1926.

3. Neither the actual decision below, nor the "broader grounds" given therefor (page 83 of record) which may have been dicta, were erroneous. But even if they were it would not follow that they should be reviewed by this court.

If the actual decision were to be thought erroneous, the supposed error comes on the extremely narrow issue whether the powers of the respondents with respect to rates and with respect to taxation were, under the circumstances of this unique case, "essentially governmental." We question whether this Court will desire to review that issue for the purpose of reaching a point where for the first time the "broader grounds" of the decision (page 83) might be considered for review.

Miller v. *McCaughn,* 27 Fed. (2nd) 128, involved an income tax upon compensation paid, out of a fund contributed by surety companies, to an attorney appointed by a probate court (without statutory authority) as standing auditor to ascertain the worth of companies desiring to go surety on probate bonds. It needs little effort to distinguish such a case from that of a primary administrative state officer.

As for the source of the compensation, the position taken in the present decision (page 84 of record) is clearly right. From whatever source derived, the statutory compensation of a public officer remains "the means by which his services are procured and retained." See *Indian Motocycle Co.* v. *United States,* 283 U. S. 570, 577.

Moreover, the burden of the salaries fell, in the last analysis, upon the Commonwealth which at the end of public operation was to take any gain and bear any loss. See Section 13, Appendix at page 20, infra. The decision, upon this narrow question of Massachusetts law, is not shown to be in conflict with any decision of a Massachusetts court or of any other court.

The latter comment applies as well to what is possibly intimated with respect to the status of the respondents (pages 9-10 of petition).

Boston Elevated Ry. Co. v. *Malley,* 288 Fed. 864, involving a federal excise tax on water transportation rates (an entirely sound decision containing on page 870 some rather inconsistent expressions) and *Boston Elevated Ry. Co.* v. *Malley,* 24 Fed. (2nd) 758, involv-

ing capital stock tax on the Railway Company, seem quite clearly not to have been (as the petitioner asserts) overruled by the present decision. It may be noted in passing that the decision makes no reference to them and that the opinion was written by the same judge who decided the second Malley case.

With respect to the essentially governmental character of the respondents' powers over rates and services, and their functions in connection with taxation, it seems sufficient to invite comparison between the provisions of the Massachusetts statute (Appendix, infra, pages 16-21), the decision of the court below (page 83 of record), and the labored language of the petition on the point (pages 11-12 of petition).

Over rates, services and facilities, the jurisdiction of the respondents was absolute,—"exclusive and . . . not subject to the approval, control or direction of any other state board or commission" (page 16, Appendix infra). The petitioner, upon the pleadings in the present case, admitted that

> "The jurisdiction of the Public Service Commission of the Commonwealth with respect to fares . . . and facilities and services of the Boston Elevated Railway was terminated and transferred to said Board of Trustees." (Pages 6 and 11 of record.)

also that

> "by virtue of said Chapter 159 said Board of Trustees became . . . a special public service commission in respect to the Boston Elevated Railway Company." (Pages 56 and 62 of record.)

The fact that the basis for rate making was prescribed by the act does not make the functions of the respondents in administering the legislative mandate any the less "essentially governmental." The authority of the trustees was not "essentially the same" as that given the company in the event of the resumption of private operation, when the company was to become "subject to public regulation and supervision" (page 21, Appendix infra) with certain limitations with respect to the net result of regulation upon revenues.

As to taxes, the trustees did more than "certify the amount of any deficit." They actually apportioned the burden (page 21, Appendix infra).

The exact extent to which the respondents exercised discretion is hardly decisive. The acts of a primary state officer are quite as governmental when he performs a duty which the legislature has defined with precision as when he exercises a delegated discretion.

And we repeat:—unless the court wishes to review this narrow issue resting primarily upon a construction of the Massachusetts statute, or the issue with respect to the source of the compensation, in the expectation of reaching a conclusion different from that of the court below, there is no issue presented by the argument in the petition competent to alter the outcome of the case.

The present case is not at all similar to *Cleveland Railway Co.* v. *Commissioner,* 36 Fed. (2nd) 347 involving an income tax upon a public utility corpora-

tion, privately operated for private profit under certain special city ordinances.

4. It seems rather doubtful whether the actual decision in this case, or even its "broader grounds," will "greatly increase the field of exemption" from federal taxation. We rather think that it will merely keep the Treasury Department from trying to circumscribe the constitutional principle, which seems to it less worthy of regard than the instant getting of revenue.

However, the principle is of equal application, as between the states and the nation,—see *Indian Motocycle Co.* v. *United States,* 283 U. S. 570, 575,—and it may be the extending activities of the federal government will at least, under the decision, be exempt from state taxation, *so far as concerns the compensation of primary administrative officers engaged in carrying out an act of congress and the policies therein embodied.*

Such cases as *Lucas* v. *Howard,* 280 U. S. 526 and *Lucas* v. *Reed,* 281 U. S. 699 cannot legitimately be described as "similar" to the present case. Those two cases (and the others cited at the bottom of page 13 of the petition) involved special services rendered by various persons, hardly to be viewed as employees and certainly not as public officers, and in no case was there any genuine participation in government. The present respondents were primary public officers, the sole administrators of a statutory policy, and, among other things, were pro tanto Public Utility Commissioners and a Board for the Apportionment of Taxes.

Reverting to the criteria of Rule 38, Paragraph 5(b).

1. The decision does not conflict with that of any other Circuit Court of Appeals on the same matter, for none of the decisions referred to were cases involving an income tax upon the compensation of an incumbent of a primary administrative office.

2. The decision, so far as it relates to local law, rests upon issues important only in a narrow context and not even suggested to be at variance with the decisions of local courts.

3. No question of general law is involved.

4. The constitutional question (raised only upon the "broader grounds" of the decision) whether the salaries of public officers may be taxed or not, dependent upon whether their functions are "essentially governmental" or not, may be an important one, but the decisions of this Court have over and over again declared the exemption in absolute terms and the issue can hardly be viewed as undecided merely because the Department has undertaken to draw some erroneous conclusions from *Flint* v. *Stone Tracy Co., supra,* and *South Carolina* v. *United States, supra.*

5. Neither the decision nor its "broader grounds" are in "probable conflict" with applicable decisions of this court.

6. Of the grounds adequate to sustain the actual decision, without embarking upon the "broader grounds," the only one which the petition really challenges is, that the powers of these particular public officers with

respect to rates and taxation were "essentially governmental." This issue alone, arising upon this unique legislation, is not of sufficient general bearing to merit review. And it is quite clear from page 14 of the petition that the petitioner is really seeking review only of the dicta referred to above as the "broad grounds."

It is respectfully submitted that the petition for a writ of certiorari should be denied.

J. COLBY BASSETT,
MELVILLE FULLER WESTON,
STANLEY R. MILLER (Pro se),
Attorneys for Respondents.

POWERS & HALL
Of Counsel

APPENDIX

SPECIAL ACTS, 1918

CHAPTER 159

[Italics ours]

THE COMMONWEALTH OF MASSACHUSETTS

IN THE YEAR ONE THOUSAND NINE HUNDRED AND NINETEEN

AN ACT

To provide for the Public Operation of the Boston Elevated Railway Company

Be it enacted by the Senate and House of Representatives in General Court assembled, and by the authority of the same, as follows:

SECTION 1. *The board of trustees* of the Boston Elevated Railway Company is hereby created, to consist of five persons *to be appointed by the governor, with the advice and consent of the council.* The persons so appointed *shall be sworn before entering upon the performance of their duties; shall own no stock or other securities of the Boston Elevated Railway Company* or of any company owned, leased or operated by it; *shall serve for the term of ten years* from the date when they assume the management of the company as hereinafter provided and until their successors are duly appointed and qualified, and each *shall receive from the company as compensation for his services five thousand dollars annually.* In case of any vacancy in said board by reason of death, resignation or otherwise, the governor, by and with the consent of the council, shall fill the vacancy. The board shall designate one of the trustees so appointed to serve as chairman. *Any member of the board may be removed for cause by the governor, with the advice and consent of the council.*

Said trustees shall not be considered public officers within the meaning of section twenty-five of chapter five hundred and fourteen of the acts of nineteen hundred and nine, but shall be subject in all other respects to the provisions of said section to the same extent as are the directors of the Boston Elevated Railway Company, but said section shall not apply to recommendations by the governor to said trustees. The provisions of section one of chapter seven of the Revised Laws shall not apply to the said board.

* * * *

SECTION 2. Said board of trustees, hereinafter called the trustees, *shall manage and operate the Boston Elevated Railway Company* hereinafter called the company, and the properties owned, leased or operated by it, for a period of ten years, commencing on the first day of the month next after their appointment and qualification, and subject to the provisions of this act, *shall take and have possession of said properties in behalf of the commonwealth during the period of operation,* and, for the purposes of this act, shall, except as is otherwise provided in this act have and may exercise all the rights and powers of said company and its directors, and, upon behalf of said company, shall receive and disburse its income and funds. They shall have the right to appoint and remove in their discretion the president, treasurer and clerk of the corporation, and all officers of the company other than the board of directors. They *shall have the right to regulate and fix fares,* including the issue, granting and withdrawal of transfers, and the imposition of charges therefor, and *shall determine the character and extent of the service and facilities to be furnished, and in these respects their authority shall be exclusive and shall not be subject to the approval, control or direction of any other state board or commission.*

In the management and operation of the said company and of the properties owned, leased or operated by it, as authorized by this act, the trustees and their agents, servants and employees shall be deemed to be

acting as agents of the company and not of the commonwealth, and the company shall be liable for their acts and negligence in such management and operation to the same extent as if they were in the immediate employ of the company, but said trustees shall not be personally liable. A majority of the board shall constitute a quorum for the transaction of business, and the action of a majority of those present at any meeting shall be deemed the action of the trustees.

Nothing herein contained shall be held to affect the right of the commonwealth or any subdivision thereof to tax the company or its stockholders in the same manner and to the same extent as if the company had continued to manage and operate its own property.

* * * *

SECTION 5. The Boston Elevated Railway Company shall, prior to or at the time of its acceptance of this act, provide for raising three million dollars in cash by the issue of preferred stock at not less than the par value which shall be one hundred dollars per share. *The issue of said stock shall not require the approval of the public service commission,* but if the remaining sections of this act fail to take effect as provided in section eighteen, such issue and the subscription thereto shall be null and void.

One million dollars shall be set aside as a reserve fund to be used for the purposes hereinafter specified, and the remaining two million dollars shall be subject to the disposition of the trustees to pay for the cost of additions and improvements to the company's property.

SECTION 6. The trustees *shall from time to time, in the manner hereinafter provided, fix such rates of fare as will reasonably insure sufficient income to meet the cost of the service,* which shall include operating expenses, taxes, rentals, interest on all indebtedness, such allowance as they may deem necessary or advisable for depreciation of property and for obsolescence and losses in respect to property sold, destroyed, or abandoned, all other expenditures and charges which under

the laws of the commonwealth now or hereafter in effect may be properly chargeable against income or surplus, fixed dividends on all preferred stock of the company from time to time outstanding, and dividends on the common stock of the company from time to time outstanding at the rate of five per cent per annum on the par value thereof during the first two years, five and one half per cent per annum on the par value thereof during the next two years and six per cent per annum on the par value thereof during the balance of the period of public operation. Dividends upon the common shares shall be payable quarterly, but no dividends shall be paid upon such common shares in excess of the rates herein specified. The first payment shall be made at the expiration of six months from the commencement of public operation, and the total of the first three quarterly dividend payments shall be five per cent on the par value of the common stock.

SECTION 7. The trustees *shall, within sixty days after their appointment and qualification, fix and put in operation rates of fare which in their judgment will produce sufficient income to meet the cost of service* as defined in section six, and within sixty days thereafter shall adopt and publish a schedule of eight different grades of fare, of which four shall be below and four above the rate of fare first established; and whenever by reason of any change in the existing rate of fare there are less than four grades, either above or below the rate then in force, the trustees shall forthwith adopt and publish a schedule of additional grades of fare so that there shall always be not less than four grades of fare above and below the existing rate of fare.

If at any time the trustees shall be of opinion that said rates of fare or schedule should be changed, either with regard to the method or basis upon which the fares and transfer privileges are established, or because the steps between the different grades are too small or too great, or for any other reason, the trustees may adopt, publish, and put in effect new schedules or rates of fare

to take the place of the existing schedule or rates of fare.

SECTION 8. The reserve fund shall be used only for the purpose of making good any deficiency in income as provided in section nine or for reimbursing the commonwealth as provided in sections eleven and thirteen, and until such use, may be invested in income-producing securities in the discretion of the trustees, and all income or interest received thereon shall be treated as part of the general income of the company.

SECTION 9. Whenever the income of the company is insufficient to meet the cost of service as herein defined, the reserve fund shall be used as far as necessary to make up such deficiency, and whenever, on the other hand, such income is more than sufficient to meet the cost of the service, the excess shall be transferred to and become a part of the reserve fund.

* * * *

SECTION 11. *If,* as of the last day of June in the year nineteen hundred and nineteen, or the last day of any December or June thereafter, *the amount remaining in the reserve fund shall be insufficient to meet the deficiency mentioned in section nine, it shall be the duty of the trustees to notify the treasurer and receiver general of the commonwealth of the amount of such deficiency, less the amount, if any, in the reserve fund applicable thereto, and the commonwealth shall thereupon pay over to the company the amount so ascertained.* Pending such payment it shall be the duty of the trustees to borrow such amount of money as may be necessary to enable them to make all payments, including dividend payments, as they become due. *If,* as of the last day of any June or December thereafter during the period of public operation, *the reserve fund shall exceed the amount originally established, the trustees shall apply the excess, so far as necessary, to reimbursing the commonwealth* for any amounts which it may have paid to the company under the provisions hereof, and the commonwealth shall thereupon distribute the amount so received among the cities and

towns in which the company operates, in proportion to the amounts which they have respectively been assessed as provided in section fourteen.

In order to meet any payment required of the commonwealth under the provisions of this section the treasurer and receiver general may borrow at any time, in anticipation of the assessments to be levied upon the cities and towns, such sums of money as may be necessary to make said payments, and he shall repay any sums so borrowed as soon after said assessments are paid as is expedient.

* * * *

SECTION 13. It shall be the duty of the trustees to maintain the property of the company in good operating condition and to make such provision for depreciation, obsolescence and rehabilitation, that, upon the expiration of the period of public management and operation, the property shall be in good operating condition. *If the period of public management and operation expires,* control of the property shall then revert to the company, *and if at that time the reserve fund shall be less than the amount originally established because the income during the period of public management and operation has been insufficient to pay the cost of the service, the commonwealth shall forthwith pay over to the company an amount sufficient to restore it to its original amount and if the amount in said reserve fund is then in excess of the amount originally established and any amount required to meet the cost of the service to the expiration of such period, such excess shall be paid into the treasury of the commonwealth* and distributed among the cities and towns in which the company operates in the same proportions as the assessments provided for by section fourteen.

SECTION 14. *In case the commonwealth shall be called upon to pay to the trustees or the company any amount under the provisions of sections eleven and thirteen, such amount* with interest or other charges incurred in borrowing money for the purpose *shall be assessed upon the cities and towns in which the com-*

pany operates by an addition to the state tax next thereafter assessed in proportion to the number of persons in said cities and towns using the service of the company at the time of said payment, *said proportion to be determined and reported to the treasurer and receiver general by the trustees from computations made in their discretion for the purpose.*

SECTION 15. Upon the termination of the period of public management and operation, the company shall manage and operate the property and may fix and collect such just and reasonable fares as will produce an income sufficient to pay the reasonable cost of the service as defined in section six, including dividends upon the common stock from time to time outstanding of six per cent per annum on the par value thereof but no more, and may establish schedules of fares which shall automatically increase or decrease in the same manner as is authorized in the case of the trustees: *provided,* that the commonwealth shall be under no liability to make any payments to the company by reason of any deficiencies in income accruing after the discontinuance of public operation. *The company shall thereafter be subject to public regulation and supervision* in such manner as may be determined by the general court, but such regulation and supervision shall not be exercised so as to reduce the income below the reasonable cost of the service as defined in this act.

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In the Supreme Court of the United States

OCTOBER TERM, 1934

No. 17

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

vs.

LELAND POWERS, EXECUTOR, ET AL.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIRST CIRCUIT

BRIEF FOR THE RESPONDENTS

I. OPINIONS BELOW.

The decision of the Board of Tax Appeals (R. 17) and the opinion of the Circuit Court of Appeals (R. 57) are reported respectively in 26 B.T.A. 1381 and 68 F. (2d) 634.

II. JURISDICTION OF THIS COURT.

The case comes before this Court upon writ of certiorari granted May 14, 1934 (R. 61) under Sec. 240 (a) of the Judicial Code as amended by Act of February 13, 1925.

III. STATEMENT.

The statement in the petitioner's Brief purports to be a summary of "the facts as found by the Board of

Tax Appeals," but most of it is the petitioner's own resumé of certain provisions of the Massachusetts statute—Special Acts, 1918, Chapter 159—which created the offices held by the respondents. The Board of Tax Appeals, in its opinion, quoted verbatim from this statute (R. 18-21), supplying italics to emphasize its own point of view.

The cases were heard upon agreed facts which included by reference those facts, alleged in the petitions, which the Commissioner's answers had admitted (R. 35, 36, 53-6). It is not controverted that each petitioner was duly appointed, duly qualified, acted, and received the statutory compensation. The case turns rather upon the character of the office and of the duties which pertained to it; and the single ultimate issue is whether the Federal Government may constitutionally levy an income tax upon that compensation.

There are set out as *Appendix A* (page 42 *infra*) excerpts from the petitions filed with the Board of Tax Appeals, and from the stipulations of agreed fact, to illustrate how the issue was framed before the Board. The facts stated in these excerpts from the petitions were, as there appears (page 43 *infra*), admitted in the answers filed by the present petitioner.

It may be of interest, in examining these excerpts, to compare the descriptions of the respondents' functions, to which the petitioner was then willing to agree, with the characterizations which are put forward in his present brief.

Another circumstance, to which the petitioner now seems not to refer, is that it was expressly agreed as a fact in the Miller cases that the respondent was an officer of the Commonwealth of Massachusetts (R. 53, 56) and that a like agreement was in substance present in the other three cases—"The office . . . was created." (R. 35, 36.)

IV. Relevant Statutes.

No relevant portion of any applicable Revenue Act undertakes to deal with the constitutional principle of exemption which these cases involve. It is conceded that, but for that principle of exemption, the taxes would effectively be imposed by those provisions of the Revenue Acts of 1926 and 1928 to which the petitioner refers.

The Treasury regulation which purports to define and circumscribe the constitutional principle reads as follows:—

> "*Compensation of State Officers and Employees.*
>
> Compensation paid to its officers and employees by a State or political subdivision thereof for services rendered in connection with the exercise of an essential governmental function of the State or political subdivision, including fees received by notaries public commissioned by States and the commissions of receivers appointed by State Courts, is not taxable. Compensation received for services rendered to a State or political subdivision thereof is included in gross income unless (a) the person receives such compensation as an officer or employee of a State or political subdivision, and

(b) the services are rendered in connection with the exercise of an essential governmental function. But see section 1211 as to 1924 and prior years."

Treasury Regulation 69, Art. 88, and see also *Treasury Regulations* 74 and 77, Art. 643, being, so far as material, substantially the same as above.

The significant provisions of *Massachusetts Special Acts* 1918, *Chapter* 159, are set out as *Appendix B* at page 47 *infra,* with certain portions thereof shown, for emphasis, in italics.

V. Argument.

A. Summary by way of Introduction.

The respondents respectfully contend that the compensation received by them as members of the Board of Trustees of the Boston Elevated Railway Company was not subject to the imposition of a Federal income tax. This contention is not based upon any provision of the Revenue Acts purporting to grant such an exemption, for the relevant Acts are silent with respect thereto. Neither is the contention really rested upon any departmental regulation, for such regulations are hardly competent to increase or diminish the scope of a principle which is exclusively of constitutional derivation. The claim of exemption rests rather upon a constitutional principle, early developed by this Court and ever adhered to, existing for the mutual protection of the states and the nation, and of which the respondents are but the casual and incidental beneficiaries.

There is no intimation that one sovereignty is to be favored over the other; and it follows, therefore, that the ordinary rule of construction, requiring statutory grants of exemption to be strictly construed against the taxpayer, can hardly be apposite. The Board of Tax Appeals seemed to apply such a rule of construction (R. 23); but, of the cases cited by it, one (*Heiner* v. *Colonial Trust Co.*, 275 U. S. 232) related solely to the construction of a statute; another (*Pacific Company, Ltd.* v. *Johnson*, 285 U. S. 480) related to a state constitutional provision with respect to tax-exempt bonds; while the language of the third case but illustrates the nice balance of the constitutional principle, which is to be

> "given such a practical construction as will not unduly impair the taxing power of the one or the appropriate exercise of its functions by the other" (government).
>
> *Susquehanna Power Co.* v. *State Tax Commission*, 283 U. S. 291, 294.

It would seem to follow, also, that the case of *U. S.* v. *Dakota-Montana Oil Co.*, 288 U. S. 459, 466, referred to by the petitioner, is beside the point for (a) the issue in that case turned upon the provisions of a statute; (b) neither a statute nor a regulation can alter or circumscribe a principle which is solely of constitutional derivation; and (c) the Revenue Acts do not even attempt to deal with the constitutional principle of exemption, with which the present case is concerned, and the re-enactment of a Revenue Act can hardly be given

a greater significance merely because of the Treasury Department having tried in the interim to deal with the subject by regulation.

The respondents as trustees of the Boston Elevated Railway Company were public officers of the Commonwealth of Massachusetts. Moreover, they were the primary executive or administrative officers, whose task was the full and complete administration of the public policy determined upon by the legislature and embodied in *Special Acts,* 1918, *Chapter* 159. As such, they were answerable for their administration of that law to no superior executive or administrative officer except as the Governor, with the advice and consent of the Executive Council, had the power of removal for cause, (pages 47-48 *infra.*)

Primary executive or administrative officers, whether their duties be broad and general or narrow and special ones, are of, and participate in, the very frame-work of government. They are as much a part of the structure of government as the legislature which enacts the law by which their duties are established, or as the Governor who appoints them, or as the Executive Council which approves their appointments. The having of public officers to put into effect the enactments of the legislature is, of its own self, and regardless of the subject matter of those enactments, a central and essential function of government. So only does the state realize itself objectively. So only do the enactments of the legislature become translated into action.

The principle resulting from our dual system of government, that the instrumentalities, means, and operations whereby each government exerts the governmental powers belonging to it are exempt from taxation by the other, has invariably been extended to cases of the compensation of public officers and employees. Distinctions based upon differences in the subject matters of particular governmental activities have been deemed significant only in cases involving excises levied upon business transactions, or involving agencies or instrumentalities remote from the central frame-work of government.

The compensation of the respondents was exempt from tax because they were public officers of Massachusetts, directly entrusted with the administration of a law and were the single means through which the state personified itself for the fulfillment of the policy embodied in that law. Their compensation was exempt irrespective of the subject matter of the law and irrespective of the source of the compensation.

Even if, however, the nature of the respondents' duties were to be viewed as having a bearing upon the question of exemption, we shall contend that the subject matter of transportation is not so obviously and markedly "non-governmental" in character as to require, in the particular case of these respondents and in the light of all their duties, a departure from the hitherto absolute rule exempting the compensation of public officers. We shall further contend that certain fundamental duties of the respondants were, by any standard, governmental.

B. The Respondents were Public Officers of the Commonwealth of Massachusetts.

Material portions of Sections 1 to 15, inclusive, of Special Acts 1918, Ch. 159, are set forth as Appendix B at page 47, *infra*.

This act has been elaborately discussed in opinions and decisions of the Supreme Judicial Court of Massachusetts and of this Court.

Opinion of the Justices, 231 Mass. 603.
Boston v. *Treasurer & Receiver General*, 237 Mass. 403.
Chelsea v. *Treasurer & Receiver General*, 237 Mass. 422.
Opinion of the Justices, 261 Mass. 523.
Opinion of the Justices, 261 Mass. 556.
Boston v. *Jackson*, 260 U. S. 309.

Excerpts comprising the principal judicial discussions of the act are quoted at length in Appendix C at page 57, *infra*.

This statute may be summarized as follows:—

Its underlying policy (as exhibited in section 6) was to provide for the rendering of service by the Boston Elevated Street Railway under such a flexible system of rate-making as would allow the fixing of fares equal, as nearly as might be, to the cost of service; and to secure that the administration of this policy should be in the public behalf and interest. To that end it provided:—

(1) The creation of a board of public trustees to take over, in the Commonwealth's behalf, manage, and operate the Boston Elevated Street Railway under such

a mandate with respect to the equivalence of fares to the cost of service.

(2) The powers and duties committed to the board of trustees to enable them to accomplish the purposes of the legislation.

(3) The terms of the arrangement between the Commonwealth and the stockholders whereby the Commonwealth acquired the right to exercise this extraordinary degree of control over this public utility.

Various special features of the law will be referred to throughout the brief. At this point, we venture to repeat the proposition, which pervades the entire discussion,—*that the board of public trustees are the only state officers to whom the general administration of this act is committed; that all power under the act derives through them; and that they are thus, while acting within the scope of their commissions, the very eyes and hands and mind of the Commonwealth, the immediate instrumentality of its action in the premises, without which the enactment of the legislative policy would be but an idle gesture.*

It has so far appeared firmly established that the respondents were public officers of the Commonwealth. It was so decided in favor of three of the present respondents in *Winthrop Coffin*, 12 B.T.A. 702; it was so agreed between the parties in the present case (see page 3 *supra*); and it was so affirmed by the Board of Tax Appeals even in its present decision (R. 21-22).

The petitioner does not venture to make any direct attack upon this proposition, but contents himself with

saying that "Although the Trustees were appointed under and their tenure and compensation were fixed by the act, and they have been referred to as public officers, it is plain that they were not public officers in the sense of performing governmental duties;" and with frequently referring to the respondents as "agents" or "agencies" (See pages 10, 17, 20, 21, 27 of petitioner's brief). A brief consideration of the characteristics of the position of the Trustees will, we submit, overcome these "arguments by indirection."

The Trustees are appointed by the Governor, with the advice and consent of the Council; are sworn before entering upon the performance of their duties; have a fixed term of office; have a compensation fixed by law; and would be disqualified by personal interest in the Railway Company, just as in General Laws, Ch. 25, Section 3, Commissioners in the Department of Public Utilities are prohibited from having any interest in the companies which come under their jurisdiction. (Section 1 of Special Acts 1918, Ch. 159, at page 47, *infra.*)

They are to have possession of the properties *"in behalf of the Commonwealth* during the period of *public operation";* and their powers are not subject "to the approval, control or direction of any *other* state board or commission." (Section 2 at pages 48-49 *infra.*)

Their duties are defined at great length by law.

These are not all the characteristics, but they are among the dominant ones, and the Board of Tax Appeals in the earlier case correctly stated that:

"They certainly satisfy every requirement of the definition of 'officers' as stated by the Supreme Court of the United States."

Winthrop Coffin, supra, page 706.

"An office is a public station conferred by the appointment of government. The term embraces the idea of tenure, duration, emolument and duties fixed by law. Where an office is created, the law usually fixes its incidents, including its term, its duties and its compensation."

Metcalf & Eddy v. *Mitchell,* 269 U. S. 514, 520.

Of course it was desirable to preserve the ability of private persons to sue the company, rather than the Commonwealth, for wrongs committed in the course of operating the railway, and it was accordingly provided that the Trustees in this regard should *"be deemed* to be acting as agents of the company and not of the Commonwealth," a provision upon which the petitioner now relies (pages 10-11, 13, 16, of petitioner's brief). But the special purposes of this and of certain other like provisions have been fully understood, and the effect properly limited, by the Supreme Judicial Court of Massachusetts in discussing a proposed bill which in this and other relevant respects was identical with St. 1918, Ch. 159.

"The operation and management of the Boston Elevated Railway Company during the term of the lease are to be by a board of public officers for the promotion of the general welfare, although at the same time provision is made for the conserva-

tion of the private interests of the owners of the railway company. . . .

"Under said c. 159, as amended by the proposed bill, the Boston Elevated Railway Company, although privately owned, will not be privately managed. On the contrary, it is to be managed, controlled and operated wholly by the board of trustees who are appointed by the Governor, who constitute a public board, who are for all essential purposes public officers although under said c. 159, Sec. 2, '*deemed to be* acting as agents of the company and not of the Commonwealth,' and whose duties are prescribed by a public statute enacted by the General Court pursuant to its constitutional prerogatives.

"The provision of Sec. 1 of the proposed act, to the effect that the trustees *shall not be considered* public officers within the meaning of G.L. c. 271, Sec. 40, does not impair or affect the general nature of their duties as public officers. The further provision exempting the trustees from the terms of G.L. c. 12, Sec. 3, has no bearing upon the character of their service as public officers. For all other purposes they are public officers. They perform public functions."

Opinion of the Justices, 261 Mass. 523, 542-3.
(Italics ours.)

The contrary expression found in *Boston Elevated Railway Company* v. *Malley,* 288 Fed. 864, 870, ought not, we submit, be given too much weight. It follows directly the quotation from *Boston* v. *Treasurer & Receiver General* to the effect that the trustees were public officers; it fails to give appropriate weight to the judicial construction of a state statute by the highest court of the state; it seems hardly necessary to the deci-

sion; and it was not repeated in the later case of *Boston Elevated Railway Company* v. *Malley*, 24 Fed. (2d) 758, written by the same judge who wrote the opinion of the Circuit Court of Appeals in the present case.

It is respectfully submitted that the respondents were public officers in every sense, and that the petitioner can hardly establish that their compensation is taxable merely by the use of characterizations calculated to derogate from, but without directly attacking, that status.

C. The Compensation of the Respondents, being the means by which their Services as Public Officers were procurred, was not subject to Tax.

In 1842, it was decided by this Court that the State of Pennsylvania might not levy a tax upon the emoluments of the office of captain in the United States revenue cutter service. The decision was placed upon grounds stated by the Court (at page 449) to be "applicable to exempt the salaries of all officers of the United States from taxation by the States."

Dobbins v. *Erie County*, 16 Pet. 435.

Twenty eight years later, in 1870, it was decided that the United States might not tax the compensation of a state Judge of Probate; upon grounds which conferred upon the compensation of all public officers of a state an exemption from taxation by the United States commensurate with that which had been affirmed in the Dobbins case.

Buffington v. *Day*, 11 Wall. 113.

The petitioner (at page 29 of his brief) undertakes to emphasize the *judicial* character of the office involved in the latter case; but it is to be noted that the Court, at the close of its opinion, quoted with approval its former assertion that

> "the reserved rights of the States, such as the right to pass laws; *to give effect to laws through executive action;* to administer justice through the courts, *and* to employ all necessary agencies for legitimate purposes of State Government, are not proper subjects of the taxing power of Congress." (Italics supplied.)
>
> *Veazie Bank* v. *Fenno,* 8 Wall., 533.

There has since stood, for over sixty years, unchallenged in this court so far as we know, the absolute principle that neither sovereignty could tax the compensation of a public officer of the other—"the means by which his services are procured." *Indian Motocycle Co.* v. *United States,* 283 U. S. 570, 577.

> See *United States* v. *Baltimore & Ohio R.R.,* 17 Wall. 322, 327. "The right of the States to administer their own affairs through their legislature, executive and judicial departments."
>
> *Flint* v. *Stone Tracy Co.,* 220 U. S. 107, 157-8.
>
> *Willcuts* v. *Bunn,* 282 U. S. 216, 225-6.
>
> *Indian Motocycle Co.* v. *United States,* 283
>
> *Indian Motorcycle Co.* v. *United States,* 283 U. S. 570, 577.

The decision in *Metcalf* v. *Mitchell, supra,* contains the following language (Italics are supplied and we have omitted citations):

"Just what instrumentalities of either a state or the Federal government are exempt from taxation by the other cannot be stated in terms of universal application. But this court had repeatedly held that those agencies through which either government immediately and directly exercises its sovereign powers are immune from the taxing power of the other. Thus, the *employment of officers who are to administer its laws,* its obligations sold to raise public funds, its investments of public funds in the securities of private corporations, for public purposes, surety bonds exacted by it in the exercise of its police power, are all *so intimately connected with the necessary function of government, as to fall within the established exemption;* and when the instrumentality is of that character, the immunity extends not only to the instrumentality itself but to income derived from it and forbids an occupation tax imposed on its use.

"When, however, the question is approached *from the other end of the scale,* it is apparent that not every person who uses his property or derives a profit, in his dealings with the government, may clothe himself with immunity from taxation on the theory that either he or his property is an instrumentality of government within the meaning of the rule.

"As cases arise *lying between the two extremes,* it becomes necessary to draw the line which separates those activities having some relation to government, which are nevertheless subject to taxation, from those which are immune. Experience has shown that there is no formula by which that line may be plotted with precision in advance. But recourse may be had to the reason upon which the rule rests, and which must be the guiding principle to control its operation. . . .

"While it is evident that in one aspect the ex-

tent of the exemption must finally depend upon the effect of the tax upon the functions of the government alleged to be affected by it, still the nature of the governmental agencies or the mode of their constitution may not be disregarded in passing on the question of tax exemption; for it is obvious that an agency may be of such a character or so intimately connected with the exercise of a power or the performance of a duty by the one government, that any taxation of it by the other would be such a direct interference with the functions of government itself as to be plainly beyond the taxing power.

"*It is on this principle that, as we have seen, any taxation by one government of the salary of an officer of the other,* or the public securities of the other, or an agency created and controlled by the other, exclusively to enable it to perform a governmental function (*Gillespie* v. *Oklahoma, supra*), *is prohibited.* But here the tax is imposed on the income of one who is neither an officer nor an employee of government and whose only relation to it is that of contract, under which there is an obligation to furnish service; for practical purposes not unlike a contract to sell and deliver a commodity. In such a situation it cannot be said that the tax is imposed upon an agency of government in any technical sense, and the tax itself cannot be deemed to be a interference with government, or an impairment of the efficiency of its agencies in any substantial way. . . .

"We do not suggest that there may not be interferences with such a contract relationship by means other than taxation which are prohibited. *Union P. R. Co.* v. *Peniston, supra,* at p. 36 (21 L. ed. 793), recognizes that there may. Nor are we to be understood as laying down any rule that taxation might not affect agencies of this character

in such a manner as directly to interfere with the functions of government and thus be held to be void.

"But *we do decide that one who is not an officer or employee of a state,* does not establish exemption from Federal income tax merely by showing that his income was received as compensation for service rendered under a contract with the state; *and when we take the next step* necessary to a complete disposition of the question, *and inquire into the effect of the particular tax on the functioning of the state government,* we do not find that it impairs in any substantial manner the ability of plaintiffs in error to discharge their obligations to the state, or the ability of a state or its subdivisions to procure the services of private individuals to aid them in their undertakings."

We have searched diligently and, we hope, thoroughly, to see whether the absolutism of the above language with respect to the exemption of the compensation of a state officer has been modified, and to see whether any further test of "essential governmental" quality has been applied in addition to the ascertainment of the existence of a public office, directly charged with the administration of a law; and we have found no decision which seemed to go to that extent.

The petitioner (at page 28 of his brief) seems to believe that the words, "The salary of an officer," in the foregoing quotation (page 16 *supra*) are modified by the words "exclusively to enable it to perform a governmental function." It is submitted that a reading of the entire passage does not lead to this result.

The rule of *Metcalf* v. *Mitchell* is thus restated by Chief Justice Hughes:

> *"Thus, while the salary of an officer of the state cannot be taxed by the Federal government,* the compensation paid by a state or a municipality to a consulting engineer, who is neither an officer nor an employee of government, for work on public projects, may be subjected to a Federal income tax. *Metcalf* v. *Mitchell,* 269 U. S. 514, 524, 70 L. ed. 384, 392, 46 S. Ct. 172."
>
> *Willcuts* v. *Bunn,* 282 U. S. 216, 225-6.

The proposition remains unqualified in the language of another subsequent decision:

> "It has been further adjudged that the salary of an officer of the United States is immune from state taxation because the salary is the 'means by which his services are procured and retained' and its taxation by a state would burden the exertion by the United States of powers belonging to the latter. *Dobbins* v. *Erie County,* 16 Pet. 435, 448, 449, 10 L. ed. 1022, 1027. And 'for like reasons' it has been held that the salary of a state officer is immune from Federal taxation. *Collector* v. *Day* (*Buffington* v. *Day*), 11 Wall. 113, 124, 20 L. ed. 122, 125."
>
> *Indian Motocycle Co.* v. *United States,* 283 U. S. 570, 577.

It is therefore submitted that when it appears that the respondents are members of a state board; appointed by the same authority by which the highest executive and judicial officers are appointed; installed in office upon oath; with long and certain tenure; with emolument fixed by law; entrusted with the administration of an important piece of legislation; and, what is more, with the primary responsibility to develop

administratively the details of the legislative policy embodied in that law; and subject to the mandates of no superior; it thence also appears that they are state instrumentalities of government whose compensation the Federal government may not tax.

We do not believe that it will be helpful to list here, and distinguish, one by one, the various cases which in recent years have dealt with compensation for services more remotely connected with the administration of government. They are all cases which arise in the "no-man's-land" indicated by *Metcalf* v. *Mitchell*—*"lying between the two extremes"*; while the case of the compensation of a public officer still stands *at one extreme,* among those cases which fall with certainty within the exemption. (See language quoted at page 15 *supra.*)

Concededly, the asserted principle of the exemption of the compensation of public officers is but a branch of a broader principle of non-interference; and the boundaries of the broader rule are set by the reasons for its existence.

See *Indian Motocycle Co.* v. *United States,* 283 U. S. 570, 575-6.

But we submit that the reason of the broader rule calls for the absolute principle of exemption for which we contend. Each government is entitled to exercise all its lawful powers, and to that end must have executive and administrative officers, for few, if any, laws or policies are self-effectuating merely upon the declar-

ation of the legislature. It is one thing to say that a business upon which a state embarks must remain taxable *as a business* and quite another thing to say that the power of the state to have primary executive or administrative officers—no matter for what public purpose so long as it be lawful—is subject to taxation, and hence to destruction, at the choice of the Federal government.

The three decisions upon which the petitioner places his greatest, if not really his sole, reliance are wholly distinguishable upon this ground.

Flint v. *Stone Tracy Co.*, 220 U. S. 107, related to the excise known as the "corporation tax" and the actual question involved was whether a street railway company, simply because it operated under a state charter, was exempt from the tax. No element of public ownership or operation was involved. The Court made use of the expression "essential governmental function," and said, at page 172,—

> "The true distinction is between the attempted taxation of those operations of the state essential to the execution of its governmental functions, *and which the state can only do itself*, and those activities which are of a private character. The former, the United States may not interfere with by taxing the agencies of the state in carrying out its purposes; the latter, although regulated by the state, and exercising delegated authority, such as the right of eminent domain, are not removed from the field of legitimate Federal taxation."

This case, however, contains no intimation that in the case of the compensation of a public officer, charged

directly with the administrative enforcement of a state law, there is to be applied some further test as to whether such officer is engaged in the performance of "essential governmental functions." On the contrary, the very case contains the following unqualified language:

> "The exercise of such rights as . . . the employment of officers to administer and execute the laws, and similar governmental functions, cannot be taxed by the Federal government."
>
> *Flint* v. *Stone Tracy Co., supra,* 158.

South Carolina v. *United States,* 199 U. S. 437, related to a license tax, imposed upon dealers in intoxicating liquors, and held applicable to the individual dispensers of liquors at certain state dispensaries, who were reached by the federal statute "because they were the actual sellers." No question was involved as to a tax upon the compensation of public officers charged with administering the policy of a state law—not even of a law relative to government sale of liquors. The tax was on the business, and the business, it was held, was of a private nature.

Ohio v. *Helvering,* 292 U. S. 360, presented the modern example of the situation which had existed in the South Carolina case, and it was made perfectly clear by the Court that the Federal excise was capable of reaching not merely the "actual sellers" but also the state itself, when it embarked upon the traffic in liquor which the Court held to be a business of a private nature.

We neither do, nor have need to, offer any criticism, express or implied, of these decisions. We are not contending that the street railway business was not subject to excise taxes, or that the salaries of those in the employ of the railway company were not subject to income tax. We are contending that the compensation of the primary public officers, *who were not in the employ of the corporation but who rather were, in the state's behalf, in possession of the corporation* (see section 2 at page 48 *infra*), was not taxable. And this contention is being advanced, not primarily on the ground that it is an "essential governmental function" to run a street railway, but because it is of the very essence of government to have executive and administrative officers as a means to enable the state to exercise its lawful powers at all.

We are unable to see that the present case is any more governed by anything that was said in *Ohio* v. *Helvering* than by the actual decision in that case. Of the various cases cited for the proposition that

> "when a state enters the market place seeking customers, it divests itself of its *quasi* sovereignty *pro tanto* and takes on the character of a trader so far at least as the taxing power of the Federal government is concerned,"

the case of *Georgia* v. *Chattanooga,* 264 U. S. 472, dealt with the power of the state to take by eminent domain land within its borders owned by another state and used for a railroad by that state; while the remaining cases —*Bank of United States* v. *Planters Bank,* 9 Wheat.

904; *Bank of Kentucky* v. *Wister,* 2 Pet. 318; *Briscoe* v. *Bank of Kentucky,* 11 Pet. 257; *Curran* v. *Arkansas,* 15 How. 304,—dealt with the status of certain private corporations and with the significance of their private transactions.

To this latter list might be added the case of *State of North Dakota* v. *Olson,* 33 Fed. 2d, 848, dismissed for want of jurisdiction, 280 U. S. 528; to which the petitioner refers. In each case the status of the corporation, or the significance of its transactions, or its liability to tax, was held not to have been changed by virtue of the state's participation in the enterprise through the ownership of its capital stock. No one of these cases involved directly, or indirectly, or even remotely, the taxability of the compensation of a primary administrative or executive officer of a state.

It is submitted that while the expression, "essential governmental function" has received the approval of this Court, it notwithstanding does not constitute, by itself alone, the safe starting point of a strictly deductive reasoning. It seems rather a convenient, general phrase to express in summary form certain, but not all, of the lines of distinction marked out by the cases which have expounded the constitutional principle.

Thus, for example, in *United States* v. *Baltimore & Ohio Railroad Co.,* 17 Wall, 322, it was held that the Federal government could not levy a tax upon the income received by the City of Baltimore from bonds of the Baltimore & Ohio Railroad, notwithstanding that the investment had been made and held for the primary

purpose of conferring upon the inhabitants of the city a greater prosperity through the development of the railroad. This case has stood unquestioned for over sixty years, notwithstanding that the one dissenting Justice endeavored to make with respect to municipally owned property precisely the same distinction as that which the petitioner now advances in a different connection. It illustrates the care with which the expression "essential governmental function" needs to be used. It may not have been an "essential government function" of the State of Maryland to lend money to railroads for the purpose of encouraging their development. But it was an "essential governmental function" of the state, and so of its municipal corporation, to hold its own property and to receive the income therefrom.

In the present case, the operation of a street railroad may not be an "essential governmental function." When, however, the state, within its lawful powers, has determined upon a public policy and has legislated with respect, thereto, it is of the essence of government to have some primary executive or administrative officers whereby to make that policy manifest in action. And this remains true even though the subject matter of the policy is the control or even operation of a public utility.

D. It is Immaterial that the Respondents' Salaries were paid "by the Company."

We respectfully submit that it does not matter by whom the respondents' salaries were paid so long as

they were paid in accordance with the provision made therefore in the statute creating the office. This follows from the nature of the constitutional principle itself. The compensation of a public officer is the "means by which his services are procured."

Indian Motocycle Company v *United States*, 283 U. S. 570, 577.

If the state can successfully provide that the compensation be paid out of other than public funds, the burden of the compensation is thereby held off from the public funds; but if such means fail, then the state must in the end provide for a compensation of which it bears the direct burden. In either case, the compensation remains the means by which the services are procured.

If, therefore, the Federal taxing power cannot reach a state public office, then it cannot reach the statutory compensation annexed to that office, whether the compensation be payable by the state or by someone else.

The petitioner says (brief, page 22) that "The burden of the tax here in question falls solely upon the respondents individually." In the only sense in which this expression is true, it would be equally true with respect to an income tax upon the salary of the Governor.

We know of no case where the distinction for which the petitioner contends has appeared, except, possibly, *Miller* v. *McCaughn*, 27 Fed. (2d) 128, which related to the compensation of an auditor appointed by the

Orphans Court in Philadelphia to ascertain and report upon the financial worth of companies applying to the court for leave to furnish surety bonds. There was no such office created by law, the appointment was purely a matter of convenience and the compensation was paid from a fund contributed by applying surety companies. Such a case seems wholly distinguishable.

On the other hand, the Treasury Department itself has long recognized that, in the case of a public officer, the source of the emolument fixed by law was not material. See, for example:

5 C. B. 106. (Fees of deputy sheriffs.)
II-1 C. B. 71. (Compensation of state employees under Sheppard-Towner Act.)
II-1 C. B. 72. (Fees of public administrators paid out of the estates.)
IV-2 C. B. 46. (Receivers of insolvent state banks paid out of bank assets.)

Once it is established that the constitutional principle applies,

> "It is not affected by the amount of the particular tax or the extent of the resulting interference, but is absolute."
>
> *Indian Motocycle Co.* v. *United States,* 283 U. S. 570, 575.

It is submitted that the petitioner's contentions (brief, pages 9-10, 32) with respect to the "allocation" of compensation are wholly incompatible with this principle.

The provision for the payment of the respondents' salaries "by the Company" was probably inspired by

precedent. There had been a time when the salaries and expenses of the Railroad Commissioners of Massachusetts had been raised by assessment upon the regulated companies (See R. L. chap. 111, sec. 10; Acts 1906, chap. 463, sec. 3; Acts 1909, chap. 490, Part III, sec. 9). This had also been true with respect to the Gas and Electric Light Commissioners (R. L. chap. 121, sec. 4; Acts 1909, chap. 490, Part III, sec. 9). Even today one-half of the salaries of the Commissioners in the Department of Public Utilities, together with that portion of the expenses of the Department incurred in connection with the regulation of gas, electric and water companies, are raised by assessment upon the regulated utilities.

In the present case, however, the payment "by the Company" seems more a matter of form than of substance. Under Section 13 of the act, page 54 *infra,* it was provided that, at the expiration of the period of public control, any deficiency arising from operating deficits should be made up by the Commonwealth and, on the other hand, that any surplus resulting from operations should belong to the Commonwealth. Thus, the entire period of operation is at the financial risk of the Commonwealth, and the gains, if any, belong to it. Any factor entering into the costs of the period of public control was bound to affect the net outcome to the Commonwealth. The respondents' salaries were such a factor.

That operating deficits in fact occurred and were made up by public taxation (R. 21) gives added em-

phasis, but the result should be no different even if no deficits had occurred. The salaries, by whomsoever paid, were the statutory compensation annexed to the office.

E. The Respondents were no less Instrumentalities of Government by reason of their being concerned with Transportation.

In this connection we assume that the principal reliance of the petitioner is placed upon *Flint* v. *Stone Tracy Co.*, and particularly upon the following language (italics supplied):

> "It is *no part of the essential governmental functions of a state to provide means of transportation,* supply artificial light, water, and the like. These objects are often accomplished through the medium of private corporations, and though the public may derive a benefit from such operations, the companies carrying on such enterprises are nevertheless private companies, whose business is prosecuted for private emolument and advantage. For the purpose of taxation they stand upon the same footing as other private corporations upon which special franchises have been conferred."
>
> *Flint* v. *Stone Tracy Co.*, 220 U. S. 107, 172.

To this language, when confined to the actual decision—namely, that an ordinary public utility company was not exempt from the Federal Corporation Tax—there may doubtless be no occasion to take exception. But when it is stripped from its context and used as the basis of a wholly different contention, it does not seem so secure from criticism.

To illustrate: let the assertion that "it is no part of the essential governmental functions of a state to provide means of transportation" be considered. Now one fair test of what is "essential" in government might be to inquire what governments have always done. And governments have always concerned themselves to some extent (and not merely by regulation) with providing and promoting means of transportation. The Roman roads; the inclusion in the Stat. 43 Eliz. c. 4 of "repairs of bridges, ports, havens, causeways . . . and highways"; modern road and bridge building; the Panama Canal; may perhaps come to mind.

True, transportation has changed greatly and offers problems much more complex than it once did, but it might be difficult to weigh accurately the importance of one factor of transportation in one age to one government as against that of a different one in a different age to another.

The Federal postal service would hardly be thought proprietary as distinct from governmental, but it is nothing but a specialized system of transportation which now competes with private carriers in certain respects; and the power to establish post offices is linked with the power to establish post *roads*. Constitution, Art. I, Section 8. It might be thought strange that in a government of delegated powers, the power to operate this particular transportation service is "essential," while in a government of reserved powers, the whole subject matter of means of transportation is claimed to be "non-essential."

Or take this expression from the *Flint* case: "The true distinction is between . . . those operations of the state essential to the execution of its governmental functions, *and which the state can only do itself*, and those activities which are of a private character." As a matter of pure logic, these words might warrant the conclusion that the making of war is not an essential governmental function because of historical precedent for the use of mercenaries who were hardly more than independent contractors; or the conclusion that the bureau of internal revenue is not "essential" because in certain times and places the institution of "farmers of the revenue" worked very nicely.

It may, therefore, not be surprising that, on the question whether providing means of transportation is a genuine and long established subject matter of government, the weight of the later cases, despite the dictum in *Flint* v. *Stone Tracy Co.*, seems to be in the affirmative. The cases to which we refer are collected and abstracted in *Appendix D*, at page 63 *infra*.

On the other hand, there is undoubted force to the argument that indefinite expansion of the functions of one government cannot be allowed to withdraw all activities within its borders from the taxing power of the other.

Cf. *South Carolina* v. *United States*, 199 U. S. 437, 454.

But we are not discussing the taxability of the railroad property, or of the railroad income, or of the compensation of employees of the railroad company. We are,

at this point, merely asserting that there is nothing so violently non-governmental about the subject matter of providing means of transportation as to require the modification of the absolute rule with respect to the exemption of public officers' compensation, as repeatedly stated by this Court.

In passing, there is one sense in which the words of the *Flint* case are presently apposite. One thing which "the state can only do itself," within the fair meaning of these words, is to have its own superior administrative officers through whom to act and thus effectuate in detail the policies formulated by its legislature. And the respondents were such an instrumentality.

F. From other Aspects the office of the Respondents was close to the Core of Government.

The constitutional principle upon which the respondents rely is a principle involving the exercise of fair judgment in practical affairs to the end that the unqualified powers granted by the Constitution to the Federal Government shall not be utilized to destroy or impair the equally unqualified powers reserved by the Constitution to the several states, and vice versa. This end is to be accomplished without unreasonably narrowing the scope of the taxing power of either sovereignty. The closer, therefore, the function sought to be taxed comes to the core of government, the more imperative it is that the taxing power be restrained.

This question of degree is illustrated in the decisions of this Court, but we have found no intimation therein

that there is a further question of degree *within* the class of public officers entrusted with the primary administration of laws.

If, however, it were to be assumed that there is such a further question of degree, it is submitted that the respondents are not thereby remitted to that outer circle of functions remotely connected with government, taxation of which is permissible.

This unique legislation has few parallels that we know of and it is more nearly similar to the Federal control of railroads and telephone and telegraph companies, in war time, than to any other situation upon which the courts have had occasion to pass.

See *Biscoe* v. *Tax Commissioner,* 236 Mass. 201.

The act was passed in time of war to protect the public interests against the threatened breakdown of the principal local transportation system of a large city which was both the state capital and an important and active industrial center, including many industries engaged in war work. The road had already been under public regulation of the ordinary sort, but the state of its finances imperiled its continued operation and it was not believed that such adjustments as could be made slowly under ordinary regulation would relieve the situation.

The law discloses, upon its face, that the fundamental policy determined upon was that the road should be operated at rates equivalent to cost of service. (See Secs. 6 and 7 at pages 51-52 *infra.*)

To effectuate that policy, it was felt necessary that for ordinary regulation on the part of the Commonwealth there should be substituted public management to the end that the cost of service and hence the fares should remain truly under public control. Thus it was necessary to make a trade with the owners of the road whereby, for a fixed compensation, they permitted the Commonwealth to add powers of management to those powers which the state already had by way of regulation.

There was therefore made what was in substance a lease by the Commonwealth of the railway company and its physical properties, and the company was to be run by the Commonwealth through its public officers and, in the last analysis, at the financial risk of the Commonwealth, with the burden eventually being borne by the municipalities which the railway served.

Practically all the machinery for operation was already available in the corporation and its existing staff, but it was necessary to have some public officer or officers, who should be the administrative arm of the government in the actual effectuating of the legislative policy, and in whom should be vested all ultimate administrative powers under the act. Had the legislature chosen to turn this task over to some already existing board of public officers, such as the public service commissioners or the highway commissioners, we would imagine that the present question never would have been raised by the Treasury Department. It was, however, thought best to create a new state board for the special purpose.

The new board thus created was given all the powers to effectuate all the purposes of the law, including the powers to do, with respect to this particular transportation system, all those things of a regulatory nature theretofore entrusted to the department of public utilities, and the further power to fix and determine the incidence of taxation to raise the revenues necessary to take care of any operating deficits.

By way of illustration, merely to call to mind the type of subject matter ordinarily controlled by the public service commissioners (or now by the commissioners of public utilities) but under this law administered by the board of trustees, we would mention a few of the things which the trustees were to do in the ordinary course of their duties. They fixed fares; determined questions with respect to transfers; determined the character and extent of the service and facilities to be furnished; and, within the latter category, dealt with the questions of the kind of vehicles to be operated on given lines, frequency of operation, location of stopping places, giving of new service and abandonment of old services once undertaken, building of extensions and removal of trolley tracks, poles and wires once already located, adequacy of shelters and transfer stations, speed, emergency stops, safety equipment, rules of conduct and the like.

It is thus not surprising that in the present case the government has admitted that

> "The jurisdiction of the Public Service Commission of the Commonwealth with respect to fares

> . . . and facilities and services of the Boston Elevated Railway was terminated and transferred to said Board of Trustees." (Record, page 4.)

Or that

> "Said Board of Trustees became at all times after July 1, 1918 a special Public Service Commission in respect to the Boston Elevated Railway Company." (Record, page 40.)

The general functions of public service commissions are too well known to require discussion, and, as said in *Burnet* v. *Livezey,* 48 F. (2d) 159 at 161,

> "There can be no doubt but that the commission was itself an agency of the state, performing governmental functions."

At this point we may be met with *Ohio* v. *Helvering,* and with the unquestionable doctrine that "the police power . . . applied to business activities is the power to regulate those activities, not to engage in carrying them on,"

Ohio v. *Helvering,* 292 U. S. 360,

from which it may well follow that the power which the Commonwealth of Massachusetts exerted through the respondents was not the "police power."

But we are not contending that, because a state may regulate a business under the police power, the embarking upon the business, even by the state, is an exercise of the police power. Nor that the business, when embarked upon by the state, loses *as a business* its private character or ceases to be a legitimate object of Federal Taxation. What we do seek to point out is that

(a) The public interest served by public management may be identical with that which sustains the police power.

(b) The ultimate object of assuming management may be—and in this case was——to effectuate fully one of the public purposes to subserve which the police power exists.

(c) When a public officer actually does the things which are of the essence of the regulatory power, their character is not changed by the fact that he does other and further things which are non-regulatory in character.

(d) When the assumption of management grows out of the exigencies of regulation, it cannot withdraw from the taxing power of the Federal government that which even under regulation was subject thereto; but it does not follow that the effect is to subject to the Federal taxing power that which theretofore was not subject thereto.

Lastly, in this discussion of the nature of the things which the respondents did, it is to be recalled that *among their basic powers was the power to determine the amount necessary to be raised by taxation to make up any operating deficits, and apportion the burden of taxation among the municipalities which the railway served.*

Now it hardly seems possible that the Commonwealth, in respect of its power to apportion the public burden of taxation, can lose its sovereign character. As to the exercise of this power in this instance, the Supreme Judicial Court has said as follows:

"The assessment authorized by Sec. 14 is an apportionment of one of the burdens of general taxation. It is not the levy of a betterment assessment and has nothing in common with such an assessment. The case at bar, like *Kingman, Petitioner,* 153 Mass. 566, deals 'with a legislative distribution of public burdens among different political subdivisions of the Commonwealth, and the language in it must be construed in reference to the facts to which it relates. The right to apportion public burdens among cities, towns, and counties as it deems reasonable, in reference to benefits and to other considerations which are not capable of exact estimation in money, is within the power of the Legislature under the first part of art. 4, c. 1, Sec. 1, of the Constitution, and is not the same as the right to impose and levy taxes upon individuals. It is of the same nature as the right to create, change, or abolish cities, towns, or other political subdivisions of the Commonwealth." *Sears* v. *Board of Aldermen of Boston,* 173 Mass. 71, 78. . . .

"There is no delegation of legislative power in the authorities vested in the trustees. The general principles to be observed are set forth in the statute. It is the carrying out of those principles with discretion, fidelity and wisdom that is vested in the trustees. However onerous that may be as an administrative burden, it does not partake of the nature of a legislative function. While such details might be included in the statute, no constitutional mandate is violated by leaving them to the decision of the trustees."

Chelsea v. *Treasurer & Receiver General,*
237 Mass. 422, 431.

With respect to this power, the petitioner says (brief, page 30) "The Trustees had no power to levy taxes. They could only certify the amount of any deficit to

the Treasurer or Receiver General, a mere ministerial act." This statement wholly overlooks the duty of the Trustees with respect to apportioning the burden of the tax. See Section 14 at page 55 *infra.*

In was this duty of which the Supreme Judicial Court was speaking, in the words quoted above—"However onerous that may be as an administrative burden—," and there seems to be something almost studied in the characterizations by which the petitioner endeavors to diminish the status of the respondents as public officers, the governmental significance of their duties, and the degree of discretion entrusted to them in administering the public policy embodied in the act. When he refers to them as "ministerial," we cannot but recall that the constitutional principle was first developed in a case involving a captain of a revenue cutter. It can hardly be a valid distinction that he was about the business of collecting Federal taxes rather than of apportioning the burden of state taxes.

What we have said does not seem to us inconsistent with the decisions of the district court in *Boston Elevated Railway Company* v. *Malley,* 288 Fed. 864; *Boston Elevated Railway Company* v. *Malley,* 24 Fed. (2d) 758.

The first of these cases involved the taxability of payments made under a private contract for ordinary services rendered in the course of the ordinary operation of the railway. We have had occasion to comment on some of the language of the decision at page 12, *supra.* The second case was likewise concerned

with the incidence of a tax upon the railway business. The underlying thought of both decisions seemed to be that, the statute having expressly left the business open to all forms of state taxation, it should fairly be deemed open to Federal taxation as well.

We repeat once more that we do not feel forced to contend that the railway business was non-taxable. Our contention is that the board of trustees, as the public officers through whom, under the legislature, the Commonwealth directly manifested itself in action, were a non-taxable instrumentality, so far as concerned a direct tax levied upon their compensation.

G. Summary in Conclusion.

It is of the very essence of a government to be able to personify itself in public officers, and through its executive or administrative officers to manifest in action the policies, within its lawful powers, upon which it has determined through its legislative branch. Hence a public officer, and especially a primary officer, is an essential instrumentality of government, and to have such officers is in itself an essential function of government.

This Court has on frequent occasions discussed with thoroughness the scope of the constitutional principle of exemption and has on no occasion failed to place public officers, as such, among those instrumentalities of government, which are "essential." It has never been intimated that public officers were to be classified according to the nature of the subject matter to which

their duties pertained, as essentially governmental officers, officers not essentially governmental and officers having duties partly governmental and partly not.

The compensation of a public officer is the means of obtaining his services. It has never been suggested that it is any less the means because paid by fees or from some source, other than public funds, which the state was competent to command. Still less has it ever been suggested that it is subject to an artificial "allocation" upon the basis of a classification of duties. It is wholly exempt.

The respondents were public officers and were, moreover, primary officers. The state spoke through the legislature but when it came to act, it acted first through them. Their compensation fell within the constitutional principle, notwithstanding the state procured it to be paid in the first instance out of a private fund, the integrity of which fund, however, the state had agreed to underwrite.

Upon the basis of decisions dealing solely with excise taxes levied upon business activities, and not with direct taxes levied upon public offices or the emoluments thereof, the petitioner seeks to exclude the respondents from the scope of the exemption. It is submitted that the cases are wholly distinguishable. A state cannot raise a private business to its own level; but, at its own level, it is competent to develop a public policy even with respect to its relations to a private business and it has a constitutional right to have public officers through whom to act in respect of a public policy coming within its lawful powers.

Even if the respondents' duties be scrutinized as to their subject matter, there appears no sufficient ground for making of them an exception to the heretofore absolute rule exempting from Federal taxation the compensation of public officers of a state. Governments have concerned themselves for centuries, and not by regulation alone, with the means of transportation. The respondents, while very likely not in the exercise of the "police power," dealt extensively with a common subject matter of public regulation, acted in the identical interest in which public regulation is exerted, and to the same substantial ends. They were, moreover, charged with the apportionment of a heavy burden of state taxation.

The decision of the Circuit Court of Appeals should be affirmed.

Respectfully submitted,

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APPENDIX A.

Excerpts from allegations of petitions, as admitted by Commissioner's answer; and from agreed facts.

The petitions filed with the Board of Tax Appeals contained the following averments:—

In the Powers, Coffin and Harriman petitions it was averred:—

> "5 (b) Pursuant to said Special Act the Trustees took and had possession of the property of the Boston Elevated Railway Company in behalf of the Commonwealth, appointed and removed officers of the corporation, regulated and fixed fares, including the issuing, granting and withdrawal of transfers, determined the character and the extent of the services and facilities to be furnished, issued stock, bonds and other evidences of indebtedness, determined the amount of any deficiency resulting from the operation of the railway and notified the Treasurer and Receiver General of the Commonwealth thereof, whereupon it became the duty of the Commonwealth to pay over to the company the amount so ascertained, and apportioned among the cities and towns in which the railway was operated the taxes to be assessed upon them as an addition to the State tax wherewith to pay such deficiency, all as more fully appears in said Special Act to which reference is hereby made and a copy of which will be adduced in evidence. The jurisdiction of the Public Service Commission of the Commonwealth with respect to the fares, stock and bond issues, and facilities and services of the Boston Elevated Railway was terminated and transferred to said Board of Trustees."

(R. 4 and see also 9 and 12.)

In the Miller petitions it was averred that:

"Under said Act the trustees are also given the right to regulate and fix fares, including the issue, granting and withdrawal of transfers, and the imposition of charges therefor, and to determine the character and extent of the service and facilities to be furnished and 'in these respects their authority shall be exclusive and shall not be subject to the approval, control or direction of any other state board or commission.' Powers were thus given the board of trustees which had been previously vested in and exercised by the public service commission of the Commonwealth of Massachusetts, and by virtue of said Chapter 159 said board of trustees became at all times after July 1, 1918, a special public service commission in respect to the Boston Elevated Railway Company.

"A more extended statement of the separate provisions of said Chapter 159 is here omitted in view of the former decision of this Board in the case Docket No. 17002 between the same parties, but said Chapter 159 which became effective in all its provisions is hereby attached, marked 'Exhibit B,' and made a part hereof."

(R. 40 and see also 47.)

These various averments were admitted by the Commissioner's answers, (R. 8, 11, 16, 44, 49.)

The agreed facts in the Powers, Coffin and Harriman cases contained, among other matters, the following additional material:—

"2. The office of trustee of the Boston Elevated Railway Company was created by Chapter 159 of the Special Acts of 1918 of the Commonwealth of Massachusetts, which Act was passed in May 1918 and went into full force and effect in that year, all prescribed conditions, as to acceptance by stock-

holders and the like, having been fulfilled. Said Act was in force and effect throughout the year 1927. For the general background in fact of this legislation, reference may be made to the various decisions and opinions of the Supreme Judicial Court of Massachusetts and the United States Supreme Court wherein the same is discussed, cited in the decision of the Board in the case of *Winthrop Coffin* v. *Commissioner of Internal Revenue,* 12 B.T.A. 703.

"4. If material, the Commonwealth in the year 1919 became required, under the terms of said Act and especially section 11 thereof, to pay over to the Board of Trustees of the Boston Elevated Railway Company the sum of $3,980,151.67. This amount was determined by the Board of Trustees of the Boston Elevated Railway Company and by them apportioned among the cities and towns in which the railway was operated. No reimbursements were made to the Commonwealth on account of said payment prior to 1922 nor in the year 1924. Operations during the years down to and including 1928 did not result in an excess sufficient to enable the full reimbursement of the $3,980,151.67 to the Commonwealth.

"6. The tax return of the petitioner's decedent for the year in question may be placed in evidence. The said Chapter 159 of the Special Acts of 1918 of the Commonwealth of Massachusetts may be judicially noticed, and as well any other pertinent provision of Massachusetts or United States law."

(R. 35, 36.)

The agreed facts in the Miller cases contained, among other matters, the following:—

"Chapter 159 of the Special Acts of 1918 became duly operative by the performance of all condi-

tions upon the happening of which the Act was to take effect and was in operation during the years of 1926 and 1927. The petitioner, as a member of the board of trustees of said Boston Elevated Railway Company, created by and under said Chapter 159, was engaged during said years 1926 and 1927 in exercising and performing the several powers and duties bestowed upon said board of trustees by said Chapter 159.

"Said Act transferred to the board of trustees powers of management and operation previously vested in the board of directors of the private corporation. The powers thus transferred include the right to make contracts in the name of the corporation; to receive and pay out all income or other moneys to which it is entitled; to issue stock, bonds or promissory notes of the company; and to appoint and remove all officers of the company other than the board of directors.

"Under said Act the trustees are also given the right to regulate and fix fares, including the issue, granting and withdrawal of transfers, and the imposition of charges therefor, and to determine the character and extent of the service and facilities to be furnished and 'in these respects their authority shall be exclusive and shall not be subject to the approval, control or direction of any other State board or commission.' Powers were thus given the board of trustees which had been previously vested in and exercised by the public service commission of the Commonwealth of Massachusetts.

"The Board of Tax Appeals, or any tribunal dealing with the petition in the above entitled case, may take judicial notice of, and there are incorporated herein by reference, said Chapter 159 of the Special Acts of Massachusetts for 1918 and the statements of fact so far as pertinent in the vari-

ous decisions and opinions of the United States Supreme Court, of the Supreme Judicial Court of Massachusetts, and of the Board of Tax Appeals, wherein said Act is discussed, and any other public laws of the United States or the Commonwealth of Massachusetts pertinent hereto; and also any additional matter contained in the taxpayer's petition and admitted by the respondent's answer filed herein."

(R. 54, and see also 56.)

APPENDIX B.

SPECIAL ACTS, 1918.

CHAPTER 159.

[Italics ours.]

THE COMMONWEALTH OF MASSACHUSETTS.

IN THE YEAR ONE THOUSAND NINE HUNDRED AND NINETEEN.

AN ACT.

To provide for the Public Operation of the Boston Elevated Railway Company.

Be it enacted by the Senate and House of Representatives in General Court assembled, and by the authority of the same, as follows:

SECTION 1. *The board of trustees* of the Boston Elevated Railway Company is hereby created, to consist of five persons *to be appointed by the governor, with the advice and consent of the council.* The persons so appointed *shall be sworn before entering upon the performance of their duties; shall own no stock or other securities of the Boston Elevated Railway Company* or of any company owned, leased or operated by it; *shall serve for the term of ten years* from the date when they assume the management of the company as hereinafter provided and until their successors are duly appointed and qualified, and each *shall receive from the company as compensation for his services five thousand dollars annually.* In case of any vacancy in said board by reason of death, resignation or otherwise, the governor, by and with the consent of the council, shall fill the vacancy. The board shall designate one of the trustees so appointed to serve as chairman. *Any member of*

the board may be removed for cause by the governor, with the advice and consent of the council.

Said trustees shall not be considered public officers within the meaning of section twenty-five of chapter five hundred and fourteen of the acts of nineteen hundred and nine, but shall be subject in all other respects to the provisions of said section to the same extent as are the directors of the Boston Elevated Railway Company, but said section shall not apply to recommendations by the governor to said trustees. The provisions of section one of chapter seven of the Revised Laws shall not apply to the said board.

If the public management and operation of the railway system of the Boston Elevated Railway Company shall continue beyond the original period of ten years the governor shall, with the advice and consent of the council, at the expiration of each ten-year period during the continuance of public management and operation, appoint five successor trustees to serve for a period of ten years, and until their successors are appointed and qualified, but not exceeding the period of public management and operation. Said trustees shall assume the management and operation of the company's property on the first day of the month next following their appointment and qualification.

SECTION 2. Said board of trustees, hereinafter called the trustees, *shall manage and operate the Boston Elevated Railway Company* hereinafter called the company, and the properties owned, leased or operated by it, for a period of ten years, commencing on the first day of the month next after their appointment and qualification, and subject to the provisions of this act, *shall take and have possession of said properties in behalf of the commonwealth during the period of public operation,* and, for the purposes of this act, shall, except as is otherwise provided in this act have and may exercise all the rights and powers of said company and its directors, and, upon behalf of said com-

pany, shall receive and disburse its income and funds. They shall have the right to appoint and remove in their discretion the president, treasurer and clerk of the corporation, and all officers of the company other than the board of directors. They *shall have the right to regulate and fix fares,* including the issue, granting and withdrawal of transfers, and the imposition of charges therefor, and *shall determine the character and extent of the service and facilities to be furnished, and in these respects their authority shall be exclusive and shall not be subject to the approval, control or direction of any other state board or commission.*

In the management and operation of the said company and of the properties owned, leased or operated by it, as authorized by this act, the trustees and their agents, servants and employees shall be deemed to be acting as agents of the company and not of the commonwealth, and the company shall be liable for their acts and negligence in such management and operation to the same extent as if they were in the immediate employ of the company, but said trustees shall not be personally liable. A majority of the board shall constitute a quorum for the transaction of business, and the action of a majority of those present at any meeting shall be deemed the action of the trustees.

Nothing herein contained shall be held to affect the right of the commonwealth or any subdivision thereof to tax the company or its stockholders in the same manner and to the same extent as if the company had continued to manage and operate its own property.

SECTION 3. The trustees shall have authority to make contracts in the name and on behalf of, and to issue stocks, bonds and other evidences of indebtedness of, the company. The trustees shall cause to be paid all amounts which may from time to time become due from the company, and shall declare dividends at the appointed times upon the preferred and common stock of the company, and provide for the payment of the same.

SECTION 4. The stockholders of the company shall, as heretofore, elect a board of directors which shall, however, during the period of public operation, have no control over the management and operation of the street railway system, but its duties shall be confined to maintaining the corporate organization, protecting the interests of the corporation so far as necessary, and taking such action from time to time as may be deemed expedient in cases, if any, where the trustees cannot act in its place. The by-laws of the company shall be modified, as far as may be necessary, to conform to the provisions of this act.

By its acceptance of this act, the company and the stockholders and directors thereof shall be deemed to have assented to and authorized all issues of stock, bonds and other evidences of indebtedness which the trustees may find necessary or advisable during the period of public operation, or which may be required during the period of public operation to carry out any existing or future obligations of the company; but, notwithstanding such assent and authorization, the stockholders and directors shall from time to time take such action with respect thereto as may be requested by the trustees.

Such sum as may be deemed reasonable shall be allowed to the board of directors each year by the trustees to provide for the maintenance of the corporate organization of the company and the performance of such duties as may be necessary by the company and the directors.

SECTION 5. The Boston Elevated Railway Company shall, prior to or at the time of its acceptance of this act, provide for raising three million dollars in cash by the issue of preferred stock at not less than the par value which shall be one hundred dollars per share. *The issue of said stock shall not require the approval of the public service commission,* but if the remaining sections of this act fail to take effect as provided in section eighteen, such issue and the subscription thereto shall be null and void.

One million dollars shall be set aside as a reserve fund to be used for the purposes hereinafter specified, and the remaining two million dollars shall be subject to the disposition of the trustees to pay for the cost of additions and improvements to the company's property.

SECTION 6. The trustees *shall from time to time, in the manner hereinafter provided, fix such rates of fare as will reasonably insure sufficient income to meet the cost of the service,* which shall include operating expenses, taxes, rentals, interest on all indebtedness, such allowance as they may deem necessary or advisable for depreciation of property and for obsolescence and losses in respect to property sold, destroyed, or abandoned, all other expenditures and charges which under the laws of the commonwealth now or hereafter in effect may be properly chargeable against income or surplus, fixed dividends on all preferred stock of the company from time to time outstanding, and dividends on the common stock of the company from time to time outstanding at the rate of five per cent per annum on the par value thereof during the first two years, five and one half per cent per annum on the par value thereof during the next two years and six per cent per annum on the par value thereof during the balance of the period of public operation. Dividends upon the common shares shall be payable quarterly, but no dividends shall be paid upon such common shares in excess of the rates herein specified. The first payment shall be made at the expiration of six months from the commencement of public operation, and the total of the first three quarterly dividend payments shall be five per cent on the par value of the common stock.

SECTION 7. The trustees *shall, within sixty days after their appointment and qualification, fix and put in operation rates of fare which in their judgment will produce sufficient income to meet the cost of service* as

defined in section six, and within sixty days thereafter shall adopt and publish a schedule of eight different grades of fare above and below the existing rate of fare. above the rate of fare first established; and whenever by reason of any change in the existing rate of fare there are less than four grades, either above or below the rate then in force, the trustees shall forthwith adopt and publish a schedule of additional grades of fare so that there shall always be not less than four grades of fare above and below the existing rate of fare.

If at any time the trustees shall be of opinion that said rates of fare or schedule should be changed, either with regard to the method or basis upon which the fares and transfer privileges are established, or because the steps between the different grades are too small or too great, or for any other reason, the trustees may adopt, publish, and put in effect new schedules or rates of fare to take the place of the existing schedule or rates of fare.

SECTION 8. The reserve fund shall be used only for the purpose of making good any deficiency in income as provided in section nine or for reimbursing the commonwealth as provided in sections eleven and thirteen, and until such use, may be invested in income-producing securities in the discretion of the trustees, and all income or interest received thereon shall be treated as part of the general income of the company.

SECTION 9. Whenever the income of the company is insufficient to meet the cost of service as herein defined, the reserve fund shall be used as far as necessary to make up such deficiency, and whenever, on the other hand, such income is more than sufficient to meet the cost of the service, the excess shall be transferred to and become a part of the reserve fund.

SECTION 10. If, as of the last day of June in the year nineteen hundred and nineteen, or the last day of any September, December, March or June there-

after, the amount of the reserve fund shall exceed by thirty per cent or more the amount originally established, and during the preceding three months the income shall have exceeded the cost of the service, the trustees shall within one month thereafter put into effect the next lower grade of fare that has been adopted as provided in section seven; and if, as of any such last day of June, September, December or March, the amount of the reserve fund shall be less than seventy per cent of the amount originally established and during the preceding three months the income has been less than the cost of the service, the trustees shall within one month thereafter put into effect the next higher grade of fare, and the fare shall continue to be decreased or increased, as the case may be, subject to the same conditions, if the amount of the reserve fund is above or below said limits, as of such quarterly dates. In determining the amount of the reserve fund for the purpose of this section only, there shall first be deducted therefrom any amounts which have been paid by the commonwealth to the company under the provisions of section eleven, and for which the commonwealth has not been reimbursed.

SECTION 11. *If,* as of the last day of June in the year nineteen hundred and nineteen, or the last day of any December or June thereafter, *the amount remaining in the reserve fund shall be insufficient to meet the deficiency mentioned in section nine, it shall be the duty of the trustees to notify the treasurer and receiver general of the commonwealth of the amount of such deficiency, less the amount, if any, in the reserve fund applicable thereto, and the commonwealth shall thereupon pay over to the company the amount so ascertained.* Pending such payment it shall be the duty of the trustees to borrow such amount of money as may be necessary to enable them to make all payments, including dividend payments, as they become due. *If,* as of the last day of any June or December thereafter during the period of public operation, the *reserve fund shall*

exceed the amount originally established, the trustees shall apply the excess, so far as necessary, to reimbursing the commonwealth for any amounts which it may have paid to the company under the provisions hereof, and the commonwealth shall thereupon distribute the amount so received among the cities and towns in which the company operates, in proportion to the amounts which they have respectively been assessed as provided in section fourteen.

In order to meet any payment required of the commonwealth under the provisions of this section the treasurer and receiver general may borrow at any time, in anticipation of the assessments to be levied upon the cities and towns, such sums of money as may be necessary to make said payments, and he shall repay any sums so borrowed as soon after said assessments are paid as is expedient.

SECTION 12. Notwithstanding anything contained in this act, the public management and operation of the railway system of the company shall continue after the expiration of said ten year period upon the terms and conditions herein specified until such time as the commonwealth shall elect to discontinue such public management and operation. The commonwealth shall have the right to terminate such public management and operation, either at the expiration of the said ten year period or at any time thereafter, by appropriate legislation passed not less than two years before the date fixed for such termination.

SECTION 13. It shall be the duty of the trustees to maintain the property of the company in good operating condition and to make such provision for depreciation, obsolescence and rehabilitation, that, upon the expiration of the period of public management and operation, the property shall be in good operating condition. *If the period of public management and operation expires,* control of the property shall then revert to the company, *and if at that time the reserve fund shall be*

less than the amount originally established because the income during the period of public management and operation has been insufficient to pay the cost of the service, the commonwealth shall forthwith pay over to the company an amount sufficient to restore it to its original amount and if the amount in said reserve fund is then in excess of the amout originally established and any amount required to meet the cost of the service to the expiration of such period, such excess shall be paid into the treasury of the commonwealth and distributed among the cities and towns in which the company operates in the same proportions as the assessments provided for by section fourteen.

SECTION 14. *In case the commonwealth shall be called upon to pay to the trustees or the company any amount under the provisions of sections eleven and thirteen, such amount* with interest or other charges incurred in borrowing money for the purpose *shall be assessed upon the cities and towns in which the company operates by an addition to the state tax next thereafter assessed in proportion* to the number of persons in said cities and towns using the service of the company at the time of said payment, *said proportion to be determined and reported to the treasurer and receiver general by the trustees from computations made in their discretion for the purpose.*

SECTION 15. Upon the termination of the period of public management and operation, the company shall manage and operate the property and may fix and collect such just and reasonable fares as will produce an income sufficient to pay the reasonable cost of the service as defined in section six, including dividends upon the common stock from time to time outstanding of six per cent per annum on the par value thereof but no more, and may establish schedules of fares which shall automatically increase or decrease in the same manner as is authorized in the case of the trustees: *provided,* that the commonwealth shall be under no liability to

make any payments to the company by reason of any deficiencies in income accruing after the discontinuance of public operation. The company shall thereafter be subject to public regulation and supervision in such manner as may be determined by the general court, but such regulation and supervision shall not be exercised so as to reduce the income below the reasonable cost of the service as defined in this act.

APPENDIX C.

The following excerpts appear to be the principal judicial summaries of the legislation administered by the petitioners:

"We consider first Spec. St. 1918, c. 159. That act was in substance and effect a taking over of the Boston Elevated Railway by the Commonwealth for operation for a limited period of ten years and possibly for a longer period under some circumstances. . . . The chief design of that act was to provide by public operation for fares at rates sufficient to meet all costs of furnishing the service.

"Under modern conditions local transportation by an electric railway may be determined by the Legislature to concern the welfare and convenience of all the inhabitants of a particular district. In essence Spec. St. 1918, c. 159, was a legislative agreement for the lease to the Commonwealth of a public utility to be operated for a limited time by public officers upon the payment of fair rental on an investment made under public supervision and under laws prohibiting stock watering or other means of inflation.

"The fundamental question is whether the General Court has the right to authorize the operation of the Boston Elevated Railway Company through the trustees appointed by the Governor. It can do so if it is a public purpose. If it is a public purpose, the General Court has the same power respecting that purpose that it has respecting other purposes. Since transportation of the public such as is furnished by the Boston Elevated Railway is a public purpose, there is no imperative constitutional requirement that it must be operated by the public authorities at cost or at a profit."

Opinion of the Justices, 231 Mass. 603, 607-8, 609, 612.

"That act provides for public operation of the railway through a board of five trustees appointed by the Governor, who 'shall manage and operate the Boston Elevated Railway Company . . . and the properties owned, leased or operated by it, for a period of ten years,' and thereafter upon the same terms until such time as the Commonwealth shall elect to discontinue public management and operation, and who, subject to the provisions of the act, 'shall take and have possession of said properties in behalf of the Commonwealth,' with 'the right to regulate and fix fares,' transfers and other charges, and to 'determine the character and extent of the service and facilities to be furnished.' The railway company is required to raise $3,000,000 by the issuance of preferred stock with dividends not to exceed seven per cent, for the improvement of the property of the company and the establishment of a reserve fund. The trustees are directed to 'fix such rates of fare as will reasonably insure sufficient income to meet the cost of the service, which shall include operating expenses, taxes, rentals, interest on indebtedness, such allowance as they may deem necessary or advisable, for depreciation of property and for obsolescence and losses,' fixed dividends on preferred stock and dividends on the common stock at the rate of five per cent for the first two years, five and one-half per cent for the next two years and six per cent for the remainder of the period of public operation. If there is a deficiency between the cost of operation as thus defined and the receipts, the trustees are required to notify the Treasurer and Receiver General and the Commonwealth shall thereupon pay the amount of the deficit ascertained according to the act. The trustees are required to maintain the property of the railway company in good operating condition and to make such provision for depreciation, obsolescence and rehabilitation;

that upon the expiration of the period of public management, the property shall be 'in good operating condition,' and shall then revert to the railway company. In case the Commonwealth is called upon to make payments to the trustees to meet deficits or diminution of the reserve fund provided for in the act, such amounts shall be assessed upon the several cities and towns in which the railway company operates by addition to the State tax next thereafter assessed in proportion to the number of persons in said cities and towns using the service of the company at the time of the payments as determined by the trustees. The act contains provision for acceptance by stockholders of the Boston Elevated Railway Company, and of the West End Street Railway Company, but not by the city of Boston; that none of its provisions shall be construed to constitute a contract binding on the Commonwealth except those which define the terms and conditions under which the property shall be managed and operated by the trustees and the provisions of Sec. 13 relating to the upkeep of the railway company's property.

"Some analysis of the provisions of Spec. St. 1918, c. 159, is necessary in order to deal with the contentions that it is unconstitutional. Its general scope is indicated by its title, which is, 'An Act to provide for the public operation of the Boston Elevated Railway Company.' The accuracy of the title is confirmed by the substance of the act throughout. Its purpose is operation through public officers and not public ownership. . . . In essence this act, having been accepted by the railway companies, constitutes an agreement between th Boston Elevated Railway Company and the Commonwealth that the latter shall take over the management and operation of the railway company and shall pay therefor the amounts specified in way of compensation for the use thereof. The

public operation is undertaken by the Commonwealth, not as a source of profit, but solely for the general welfare. The main design of the act is public operation of the railway company at such rates of fare to be fixed by the trustees from time to time as shall afford revenue sufficient to defray all charges and the dividends established by the act.

"The Commonwealth, acting through the General Court, has the constitutional power to assume the management and operation of the Boston Elevated Railway Company system. The reasons may be stated briefly. It is matter of common knowledge that the passenger transportation service for Boston and its suburbs is chiefly by the means afforded by that system through lines of electric railways on the surface, by elevated structures and through tunnels and subways. Under modern conditions the nature of that transportation system as to adequacy, efficiency, speed, safety, comfort and expense and in other respects relates to the accommodation of the public and concerns the public welfare. There is no distinction in principle between the management and operation of such a transportation system by a public agency established by the Legislature and the taking over by counties, cities and towns of toll bridges and turnpikes, originally private enterprises. The validity of such takings is settled.

"It is matter of common knowledge, and has come to the attention of the court in cases to be decided, that the period after the opening of the Great War and at the time of the passage of this act was one of extraordinary difficulty and abnormal conditions for the operation of street railways."

Boston v. *Treasurer & Receiver General*, 237 Mass. 403, 410-11, 411-14, 416.

"The operation and management of the Boston Elevated Railway Company during the term of the lease are to be by a board of public officers for the promotion of the general welfare, although at the same time provision is made for the conservation of the private interests of the owners of the railway company."

Opinion of the Justices, 261 Mass. 523, 542.

"The railway company got into financial difficulty. It served the residents of Boston and other towns of the commonwealth. The general court, in the public interest, passed the special Act of 1918 to relieve the situation. In general the act provided for the appointment of trustees, who were to take the railway out of the hands of the company and operate it under the leases to the company by the city of Boston, on condition that the stockholders of the railway company accepted the provisions of the act. It is not necessary to set out what these provisions in detail are, except to say that they provide for the payment of dividends on the stock of the company, the repair and maintenance of the railway, the raising of $3,000,000 by the company for the improvement of the property and a reserve fund, and the payment of any deficit in operation out of the treasury of the commonwealth. If the commonwealth is called upon to make payments to meet deficits or diminution of the reserve fund, such amounts are to be assessed upon the several cities and towns in which the railway operates, as an addition to the regular state tax, in proportion to the number of persons in said cities and towns using the service of the company at the time of the payments, as determined by the trustees. The trustees are to fix the fares to meet the cost of service, including taxes, rentals, and interest on the indebtedness of the company, fixed

dividends on the preferred stock, and 5 per cent on the common stock for two years, 5½ per cent for the next two years, and 6 per cent for the remainder of public operation, which is for a period of ten years, and thereafter as the Commonwealth shall determine."

Boston v. *Jackson*, 260 U. S. 309, 311-12.

APPENDIX D.

The following cases would seem to indicate that even since *Flint* v. *Stone Tracy Company,* 220 U. S. 107, 172, the providing of means of transportation may have been viewed generally as an "essential governmental function."

In *Jamestown & Newport Ferry Company* v. *Commissioner,* 41 Fed. (2d) 920 (C. C. A. 1st), a ferry corporation, wholly owned by a municipality, was held to be an agency for the performance of an essential governmental function and not subject to an income tax. It is true that Sec. 213 (*b*) (7) of the Revenue Acts of 1921 and 1924 was involved, but the court did not seem to feel that the language of that section was necessarily decisive, for it placed considerable emphasis on the constitutional exemption itself.

In *United States* v. *King County,* 281 Fed. 686 (C. C. A. 9th), it was held that the Federal transportation tax could not apply to a ferry, maintained and operated by a county.

In *Frey* v. *Woodworth,* 2 Fed. (2d) 725 (D. C. E. D. Mich. S. D.), it was held that the salary of an employee of a municipally owned and operated street railway was not subject to the Federal income tax. The government sued out a writ of error which later, on the motion of the Solicitor General, was dismissed with costs. 270 U. S. 669.

See also *Moisseiff* v. *Commissioner,* 21 B. T. A. 515, involving the salary of an employee of the Delaware River Bridge Joint Commission and the Port of New York Authority.

On the other hand, the following decisions seem distinguishable:

In *City of Seattle* v. *Poe,* 4 Fed. (2d) 276 (D. C. W. D. Wash. M. D.), the court merely held that the case was not one for the issuance of an injunction against the collections of taxes.

In *Lyons* v. *Reinecke,* 10 Fed. (2d) 3 (C. C. A. 7th), relating to the compensation of an employee of the Board of Local Improvements of the City of Chicago, the declaration was held to be too vague and uncertain. (*Id.* page 7.) Further, the whole theory of the statute was that the improvements should be "of local concern, a local benefit, that may be stopped or postponed by a majority of the frontage involved." (*Id.* page 6.) Such discussion as there is of the distinction between governmental functions and business of a private nature is not particularly satisfactory.

In *Blair* v. *Byers,* 35 Fed. (2d) 326 (C. C. A. 8th), the salary of the counsel for the "Board of Water Works Trustees" of the City of Des Moines was held taxable. The tax related to years which were subject to Section 1211 of the Act of 1926 and the taxpayer was held not to have become an officer or employee within the meaning of the statute. The Court did say that "the building and operation of a water works system by municipalities constitutes the exercise of a proprietary, rather than a governmental function." (*Id.* page 327.) Reliance was, however, placed upon quotations from *South Carolina* v. *United States* and from *Flint* v. *Stone Tracy Co.,* without adequate analysis of what those cases actually decided.

In *Cleveland Railway Co.* v. *Commissioner of Internal Revenue,* 36 Fed. (2d) 347 (C. C. A. 8th), the income of a company operating a street railway system was held subject to tax in its entirety notwithstanding that its excess income over certain dividend requirements had to be made the basis of reduced fares in succeeding years. This decision is fairly within the scope of *Flint* v. *Stone Tracy Co.* The petitioner was a privately owned corporation; the city owned no part of its capital stock, derived no income from the operation of its business and paid no part of its expenses; therefore the tax could not fall upon the city or interfere with its governmental functions. (*Id.* page 349.)

SUPREME COURT OF THE UNITED STATES.

No. 17.—October Term, 1934.

Guy T. Helvering, Commissioner of Internal Revenue, Petitioner, *vs.* Leland Powers, Executor, et al.	On Writ of Certiorari to the United States Circuit Court of Appeals for the First Circuit.

[December 3, 1934.]

Mr. Chief Justice Hughes delivered the opinion of the Court.

The question presented is whether the compensation of the members of the Board of Trustees of the Boston Elevated Railway Company is constitutionally exempt from the imposition of a federal income tax. Immunity is sought upon the ground that the trustees are officers of the Commonwealth of Massachusetts and instrumentalities of its government. The Circuit Court of Appeals, reversing the decision of the Board of Tax Appeals, held in favor of the exemption. 26 B. T. A. 1381; 68 F. (2d) 634. We granted a writ of certiorari. 292 U. S. 620.

Chapter 159 of the Massachusetts Special Acts, 1918, provides for the public operation of the Boston Elevated Railway Company. The Act creates a board of five trustees, to be appointed by the Governor, with the advice and consent of the Council, for the term of ten years. The Act provides that the trustees shall be sworn before entering upon their duties; they shall own no stock or other securities of the Company and shall each receive from the Company $5,000 annually as compensation for his services. They are subject to removal by the Governor with the advice and consent of the Council.

The trustees are charged with the duty of managing and operating the Company and its properties for the period, as stated or extended, of public operation, and to that end are to have "possession of said properties in behalf of the Commonwealth". Except as otherwise stated, they are to exercise all the powers of the Company, being empowered in their discretion to appoint and remove the

president and other officers of the Company, except the directors. The trustees are authorized "to regulate and fix fares" and "to determine the character and extent of the service and facilities to be furnished". Their authority for this purpose is made "exclusive" and is not "subject to the approval, control or direction of any other state board or commission". The Act provides that the trustees and their employees shall be deemed to be acting as agents of the Company and not of the Commonwealth, and that the Company shall be liable for their acts and negligence to the same extent as if they were in the immediate employ of the Company, but that the trustees shall not be personally liable.

The Company was required, on or before its acceptance of the Act, to raise a stated amount by the issue of preferred stock in order to provide for the improvement of the property of the Company and the establishment of a reserve fund. The trustees are to fix such rates of fare as will reasonably insure sufficient income to meet the cost of service, as defined, which, in addition to operating expenditures, outlays for the required upkeep of the properties, and other amounts chargeable against income and surplus, includes fixed dividends on the preferred stock and dividends on the common stock at specified rates. Surplus income is to be transferred to the reserve fund and that fund is to be used to meet deficiencies. If it is insufficient for that purpose, the trustees are required to notify the treasurer and receiver general of the Commonwealth, and the Commonwealth is to pay the amount of the deficit ascertained according to the Act. Amounts thus paid are to be assessed upon the several cities and towns in which the Company operates. Provision is made for reimbursement out of subsequent surplus income. The Act contemplates the maintenance of the property in good operating condition and the restoration of the reserve fund, if depleted, to its original amount on the expiration of the period of public management. At that time the control of the property is to revert to the Company. It may then collect such reasonable fares as will produce an income sufficient to pay the reasonable cost of the service as defined in the Act, including specified dividends on the common stock, and the Company is then to be subject to public regulation in such manner as may be determined by the General Court, but not so as to reduce the income below the cost of the service as stated.

The tax in question was on the compensation received by the trustees for the years 1926 to 1929. It appears that in 1919 the Commonwealth paid to the Company nearly $4,000,000 as a deficiency resulting from the public operation, and that in subsequent years, up to and including 1929, the income received was not sufficient for full reimbursement.

The validity of the statute has been sustained as one enacted for a public purpose and providing for the management of the enterprise by the Commonwealth. *Boston* v. *Treasurer & Receiver General*, 287 Mass. 403, 413, 420; *Boston* v. *Jackson*, 260 U. S. 309, 314, 316. The Supreme Judicial Court of Massachusetts has characterized the "public operation" as "undertaken by the Commonwealth, not as a source of profit, but solely for the general welfare". *Boston* v. *Treasurer & Receiver General, supra.* The trustees are the administrative agents of the Commonwealth in this enterprise, and we may assume, as the Circuit Court of Appeals has held, that the trustees come within the general category of "public officers" by virtue of their appointment by the Governor, with the advice and consent of the Council, and their tenure and duties fixed by law.[1] *United States* v. *Hartwell*, 6 Wall. 385, 393; *Metcalf & Eddy* v. *Mitchell*, 269 U. S. 514, 520. See *Opinion of the Justices*, 261 Mass., pp. 542, 543, 550.

While the undertaking is for the public benefit, it is still a particular business enterprise—the operation of a street railway—and the functions of the trustees are limited accordingly. The property remains in private ownership. The Act, accepted by the Company, constitutes in substance an agreement between the Company and the Commonwealth that the latter shall temporarily take over the management and operation and pay specified amounts by way of compensation. While the Commonwealth may be called upon to bear losses that may occur, if the fares as fixed prove to be insufficient, the operation by the trustees is intended to be self sustaining. The transportation service is to be rendered, as respondents' counsel say, "under such a flexible

[1]The provision of Section 1 of Chapter 159 of the Massachusetts Special Acts of 1918 that the trustees shall not be considered public officers within the meaning of Section 25 of Chapter 514 of the Acts of 1909, and that Section 1 of Chapter 7 of the Revised Laws shall not apply to the trustees, creates special limitations of such a nature as not to derogate from their general status. See Opinion of the Justices, 261 Mass., p. 543.

system of rate-making as would allow the fixing of fares equal, as nearly as might be, to the cost of service." The compensation of the trustees is undoubtedly a part of that cost. "The main design of the Act", as stated by the Supreme Judicial Court, "is public operation of the railway company at such rates of fare to be fixed by the trustees from time to time as shall afford revenue sufficient to defray all charges and the dividends established by the act". *Boston* v. *Treasurer & Receiver General, supra.* The authority given to the trustees "to regulate and fix fares", and the further authority to ascertain such losses as may be incurred, which are to be borne by the Commonwealth, are both incident to that main purpose.

The immunity sought by the trustees from payment of the federal income tax has not been granted by the Congress. The definitions of income in the federal income tax acts cover income derived "from compensation for personal service . . . of whatever kind and in whatever form paid". Revenue Acts of 1926, secs. 212 (a), 213 (a); 1928, secs. 21, 22 (a). This language is certainly broad enough to embrace the compensation of the trustees, and the immunity, if it exists, must rest upon constitutional limitation. The Treasury Regulations, manifestly in an effort to interpret and apply that limitation, provide for exemption from taxation of compensation paid by a State or political subdivision to its officers and employees only in case their services are rendered "in connection with the exercise of an essential governmental function". Treas. Reg. No. 69, Art. 88; No. 74, Art. 643; No. 77, Art. 643. But the Treasury Department could not by its regulation either limit the provisions of the statute or define the boundaries of their constitutional application.

We come then to the question whether the Congress has the constitutional power to impose an income tax upon the compensation of public officers of the character here involved. We do not regard that question as answered by mere terminology. The roots of the constitutional restriction strike deeper than that. The term "public office" undoubtedly implies a definite assignment of public activity, fixed by appointment, tenure and duties. But whether that field of activity in relation to a State, carries immunity from federal taxation is a question which compels consideration of the nature of the activity, apart from the mere creation of offices for conducting it, and of the fundamental reason for denying federal

authority to tax. That reason, as we have frequently said, is found in the necessary protection of the independence of the national and state governments within their respective spheres under our constitutional system. *Collector* v. *Day*, 11 Wall. 113, 125, 127; *Ambrosini* v. *United States*, 187 U. S. 1, 7; *Indian Motocycle Company* v. *United States*, 283 U. S. 570, 575. The principle of immunity thus has inherent limitations. *Metcalf & Eddy* v. *Mitchell*, *supra*, pp. 522-524; *Willcuts* v. *Bunn*, 282 U. S. 216, 225, 226; *Indian Motocycle Company* v. *United States*, *supra*, p. 576; *Fox Film Corporation* v. *Doyal*, 286 U. S. 123, 128; *Board of Trustees* v. *United States*, 289 U. S. 48, 59. And one of these limitations is that the State cannot withdraw sources of revenue from the federal taxing power by engaging in businesses which constitute a departure from usual governmental functions and to which, by reason of their nature, the federal taxing power would normally extend. The fact that the State has power to undertake such enterprises, and that they are undertaken for what the State conceives to be the public benefit, does not establish immunity. *South Carolina* v. *United States*, 199 U. S. 437; *Flint* v. *Stone Tracy Company*, 220 U. S. 107, 172; *Murray* v. *Wilson Distilling Company*, 213 U. S. 151, 173; *Metcalf & Eddy* v. *Mitchell*, *supra*; *Indian Motocycle Company* v. *United States*, *supra*; *Ohio* v. *Helvering*, 292 U. S. 360, 368, 369. The necessary protection of the independence of the state government is not deemed to go so far.

In *South Carolina* v. *United States*, *supra*, the State undertook to establish a monopoly of the sale of intoxicating liquors and prohibited the sale except to dispensaries to be operated by the State. The dispensers had no interest in the sales and received no profit from them. The question was whether the dispensers were relieved from liability for the internal revenue tax prescribed by the Congress for dealers in intoxicating liquors because the dispensers were agents of the State, which in the exercise of its sovereign power had taken charge of the business. While the court recognized the power of the State to undertake the enterprise, the exemption was denied, as the State could not, by engaging in a business of that sort, withdraw it from the taxing power which the Constitution vested in the national government. *Murray* v. *Wilson Distilling Company*, *supra*.

The Court reached a similar conclusion in the recent case of *Ohio* v. *Helvering, supra*, where the State had established a department of liquor control and sought an injunction to restrain the enforcement of federal statutes imposing taxes upon dealers in intoxicating liquors. The State sought to distinguish the case of South Carolina because, in Ohio, "the state-owned stores" were operated by civil service employees of the state government, and hence the question was said to concern the taxation of the State itself. The argument was unavailing and the Court rested its ruling upon the broad ground that when the State becomes a dealer in intoxicating liquors it falls within the reach of the tax as one validly imposed by the federal statute.

The method which the State may adopt in organizing such an activity cannot be regarded as determinative. If the dealers in South Carolina, or those employed to operate the state stores in Ohio, had been denominated public officers, and as such had been assigned definite tenure and duties, the same result would have been reached, as the principle involved would be equally applicable. Nor, in such a case, would the fact that the officers were entrusted with the authority to fix prices for the sales under their charge in a manner appropriately to secure the revenue needed for the enterprise, or were charged with the duty of ascertaining the losses which, if they occurred, were to be borne by general taxation, establish a material distinction. The nature of the enterprise, and not the particular incidents of its management, would control.

We see no reason for putting the operation of a street railway in a different category from the sale of liquors. In each case, the State, with its own conception of public advantage, is undertaking a business enterprise of a sort that is normally within the reach of the federal taxing power and is distinct from the usual governmental functions that are immune from federal taxation in order to safeguard the necessary independence of the State. If, in the instant case, the Commonwealth had acquired the property of the Company and had organized management of it in perpetuity by the state government, instead of temporarily, or had taken over all the street railways in all its cities for direct operation by the Commonwealth, there would appear to be no ground, under the principles established by the decisions we have cited, for holding that this would effect the withdrawal of the enterprise from the federal taxing power. And the fact that the State has here under-

taken public management and operation for a limited time, and under the particular restrictions of the agreement with the Company, cannot be said to furnish a ground for immunity.

If the business itself, by reason of its character, is not immune, although undertaken by the State, from a federal excise tax upon its operations, upon what ground can it be said that the compensation of those who conduct the enterprise for the State is exempt from a federal income tax? Their compensation, whether paid out of the returns from the business or otherwise, can have no quality, so far as the federal taxing power is concerned, superior to that of the enterprise in which the compensated service is rendered.

We conclude that the Congress had the constitutional authority to lay the tax.

Decree reversed.

A true copy.

Test:

Clerk, Supreme Court, U. S.